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RECORD.

UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

No. 15,703

TAX REVIEW.

HERMAN PASTER, PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE,
RESPONDENT.

PETITION TO REVIEW DECISION OF THE TAX COURT OF THE UNITED STATES FILED NOVEMBER 16, 1956.

The Scheffer Press, Inc.—ANdover 8-6350

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[fol. 1] DOCKET NO. 38018

Herman Paster, Petitioner,

vs.

Commissioner of Internal Revenue, Respondent.

Appearances:

For Petitioner:

Claude E. Peterson, Esq.
Sidney J. Kaplan, Esq.
Maurice Weinstein, Esq.

For Respondent:

Marvin J. Kelley, Esq.
R. C. Whitley, Esq.

DOCKET ENTRIES

1951

Dec. 17—Petition received and filed. Taxpayer notified. Fee Paid.

Dec. 18—Copy of petition served on General Counsel.

1952

Feb. 8—Answer filed by General Counsel.

Feb. 8—Request for hearing in St. Paul, Minnesota filed by General Counsel.

Feb. 12—Notice issued placing proceeding on St. Paul Calendar. Service of answer and request made.

1953

Mar. 17—Hearing set July 6, 1953, St. Paul, Minnesota.

Jul. 14, 15—Hearing had before Judge Turner on merits, entry of appearance of Sidney J. Kaplan filed, Briefs—11/23/53 and Replies—12/23/53.

Aug. 3—Transcript of hearing 7/14, 15/53 filed.

Nov. 4—Motion for extension to Jan. 23, 1954 to file original briefs and Feb. 23, 1954 to file reply

briefs filed by taxpayer. 11/6/53 granted. Original briefs due Jan. 22, 1954. Reply briefs due Feb. 23, 1954.

1954

Jan. 11—Designation of Sidney J. Kaplan to receive service of papers filed by Claude E. Peterson, first counsel.

Jan. 11—Copy of designation of counsel served on General Counsel.

Jan. 18—Brief filed by taxpayer. Copy served 1/20/54.

Jan. 22—Motion for extension to Feb. 6, 1954 to file brief, filed by General Counsel. 1/25/54 granted.

Feb. 5—Brief filed by General Counsel.

Feb 8—Copy of taxpayer's brief served on General Counsel.

Feb. 12—Motion for extension to April 9, 1954 to file reply brief, filed by taxpayer. 2/15/54 granted to April 9, 1954.

Mar. 29—Reply brief filed by taxpayer. Copy served.

Mar. 29—Motion to receive additional exhibits (Petitioner's exhibits #14 and 15 annexed thereto), filed by taxpayer. 3/30/54 copy served.

[fol. 2]

Mar. 30—Hearing set April 21, 1954, Washington, D. C. on petitioner's motion.

Apr. 2—Memorandum in lieu of appearance filed by petitioner. Copy served.

Apr. 21—Hearing had before Judge Turner on petitioner's motion to reopen to receive in evidence exhibit numbers 14 and 15. Respondent's objections to petitioner's motion filed. Copy served.

Apr. 23—Transcript of hearing April 21, 1954 filed.

May 17—Order, petitioner's motion that the proposed exhibits 14 and 15 be received in evidence and

made part of the record is denied, without prejudice, to a renewal of the motion as to the proposed exhibit 14 upon proper showing as to identification, etc., entered.

May 21—Renewal of motion to receive additional exhibit (#14) with attached affidavit filed by petitioner.

Jun. 8—Order, that the renewal motion is denied, still without prejudice to further renewal of the motion, upon submission of an adequately certified copy of the document sought to be entered in evidence, entered.

Jun. 25—Further renewal of motion to receive in evidence the attached certified photostatic copy (exhibit 14) filed by petitioner. 6/28/54 granted.

Jun. 29—Order, that document admitted in evidence and marked as petitioner's exhibit 14 on June 28, 1954, is redesignated as petitioner's exhibit 16, instead of exhibit 14, entered.

1956

Jun. 20—Memorandum findings of fact and opinion filed, Turner, J. Decision will be entered under Rule 50. 6/21/50 served.

Aug. 17—Agreed computation for entry of decision filed.

Aug. 22—Decision entered, Judge Turner, Division 8. Served 8/24/56.

Nov. 16—Entry of appearance of Maurice Weinstein, as counsel, filed.

Nov. 16—Petition for review by United States Court of Appeals, 8th Circuit, filed by petitioner.

Nov. 16—Proof of service filed.

Nov. 19—Request from Court of Appeals, 8th Circuit, for transmission of entire original record (exhibits to be retained in this office for 20 days after transmission of record), filed.

[fol. 3]

The Tax Court of the United States

(Filed in Tax Court December 17, 1951)

Herman Paster, Petitioner,

vs.

Commissioner of Internal Revenue, Respondent.

Docket Number 38018

PETITION

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency dated September 20, 1951, signed John B. Dunlap, Commissioner, by T. E. Feig, Internal Revenue Agent in Charge, St. Paul Division, and, as a basis of this proceeding alleges as follows:

1. Your petitioner is an individual taxpayer, residing at 1752 Pinehurst Avenue, St. Paul, Minnesota, who filed income tax returns for all of the years under consideration with the Collector of Internal Revenue at St. Paul, Minnesota.

2. That the notice of deficiency (a copy of which is attached and marked Exhibit A) was mailed to the petitioner by Registered mail on September 20, 1951 and was received by the petitioner on September 21, 1951.

3. That the taxes in controversy are additional income taxes for the calendar year 1944 in the amount of $40,768.14, for the calendar year 1945 in the amount of $24,588.00 and for the calendar year 1946 in the amount of $38,683.15.

[fol. 4] 4. The determination of the tax set forth above for the years specified therein in said notice of deficiency is based upon the following errors:

(a) For the calendar year 1944 the examining officers added $51,519.81 to the income reported by the taxpayer from the Mayflower Novelty Company, said amount being the income designated by said Mayflower Novelty Company as being the property of three trusts, one of said trusts being designated for each of the three following individuals: Celia Paster, wife of your petitioner, Donald Paster, son of your petitioner, and Edward Paster, son of your petitioner with Herman Paster, your petitioner and Sam Walzer, father-in-law of your petitioner named as co-trustees of each of said trusts.

(b) For the calendar year 1945 the examining officers added $33,879.66 to the income reported by the taxpayer from the Mayflower Novelty Company, said amount being the income designated to the foregoing trusts, each in the amount of $11,293.22.

(c) For the calendar year 1946 the examining officers added $39,223.26 to the income reported by the taxpayer from the Mayflower Novelty Company, said amount being the income designated to the foregoing trusts, each in the amount of $13,074.42. In addition to the above addition to income, the examining officers disallowed a deduction of $7,000.00 claimed by the taxpayer as a payment to eliminate competition for the year 1946.

5. The issue upon which this petition is based is as follows: Is the additional income from the Mayflower Novelty Company properly taxable to your petitioner as set forth in the report of the examining officers or, as is contended by the petitioner, is the said income taxable to the beneficiaries of the aforementioned trusts, as reported by them in their individual income tax returns?

[fol. 5] 6. The facts upon which the petitioner relies as a basis for this proceeding are as follows:

(a) The Mayflower Novelty Company, later designated as Mayflower Distributing Company, was engaged in the business of buying, selling, and distributing coin operated amusement machines. It was unincorporated and filed information returns with the Collector of Internal Revenue on forms 1065 designated as partnership returns. Its books were kept on a fiscal year basis, ending January 31, of each of the years in question. Prior to January 31, 1943, the capital invested in said business was that of S. H. Taran, S. H. Taran Trust, and J. H. Nilva. A large investment was required to carry on the operation of said business. The business was deemed hazardous because of legislation and potential legislation barring the operation and distribution of many of the devices handled by the business.

(b) Your petitioner, Herman Paster, was employed as General Manager of the business, for which he received a salary of $5,200.00 per annum, plus 20% of the profits up to January 31, 1943. He had no investment, no tenure of office, no interest in the assets of the Company, and no personal liability for the debts and obligations of the business.

(c) As of January 31, 1943, one Morris Roisner, who had previously participated in the profits of the business, severed his connection with said business, at which time there was an accumulation of profits owing to him. At that time there was also owing to the petitioner from said business, for his percentage of profits for services rendered, a sum of money in excess of $30,000.00.

(d) As of January 31, 1943, a new agreement was entered into between S. H. Taran and your petitioner to the effect that, in consideration of the investment of three sums of $10,000.00 each, commencing with February

1, 1943 [fol. 6] the petitioner was to continue his employment and the same relationship with the business for a consideration of $5,200.00 salary plus 14% of the net earnings of the Company and in consideration of the investment of each sum of $10,000.00, there would be credited and paid 7% of the net profits of the business.

(e) On the 29th day of December, 1942, Herman Paster assigned $10,000.00 of the amount owing him by said business to Herman Paster and Sam Walzer as Trustees for Celia Paster; $10,000.00 of said amount to Herman Paster and Sam Walzer as Trustees for Donald Paster, and $10,000.00 of said amount to Herman Paster and Sam Walzer as Trustees Edward Paster. On said 29th day of December 1942, Herman Paster, as Donor, entered into three identical trust instruments as designated above, with Sam H. Walzer and Herman Paster as Trustees. A copy of the said Trust for the benefit of Celia Paster, is attached hereto as exhibit B.

Wherefore, the petitioner prays that this Court may hear the proceeding and determine that there is no deficiency due from the petitioner for income taxes in the calendar years 1944, 1945, and 1946, resulting from the income designated by the examining officers as being taxable to the petitioner rather than to the beneficiaries of the several trusts above set forth.

/s/ Claude E. Petersen
Claude E. Petersen
Counsel for Petitioner,
654 McKnight Building,
Minneapolis 1, Minnesota

[fol. 7] Verification.

State of Minnesota }
County of Hennepin } ss.

Herman Paster being duly sworn says that he is the petitioner in the foregoing action; that he has read the foregoing petition and has personal knowledge of the facts set forth therein, and that he believes the statement thereof to be true.

/s/ Herman Paster
Herman Paster.

Subscribed and sworn to before me,
a Notary Public of and for the
County of Hennepin, State of
Minnesota, this 14th day of December, 1951.

/s/ Peter Skurdalswold
Notary Public Hennepin County, Minn.
My commission expires May 12, 1962.

(Statement attached to original petition omitted)

[fol. 17] Answer.

(Filed in Tax Court, Feb. 8, 1952)

Comes now the Commissioner of Internal Revenue, by his attorney, Mason B. Leming, Acting Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed by the above-named petitioner, admits and denies as follows:

1. Admits the allegations contained in paragraph 1 of the petition.

2. Except that it is denied that a complete copy of the statement attached to the deficiency notice is attached to the petition, admits the allegations of paragraph 2 of the petition.

3. Admits the allegations contained in paragraph 3 of the petition.

4. (a) to (c), inclusive. Denies that the determination of tax set forth in the deficiency notice is based upon errors alleged in subparagraphs (a) to (c), inclusive, of paragraph 4 of the petition, or upon any error.

[18] 5. Denies the allegations contained in paragraph 5 of the petition.

6. (a) Denies the allegations contained in subparagraph (a) of paragraph 6 of the petition.

(b) Except that it is admitted that petitioner received at least $5,200 and at least 20% of the profits from the Mayflower Distributing Company during periods up to at least January 31, 1943, denies the allegations of subparagraph (b) of paragraph 6 of the petition.

(c) and (d). Denies the allegations contained in subparagraphs (c and (d) of paragraph 6 of the petition.

(e) Except that it is admitted that a copy of a document labeled Exhibit "B" is attached to the petition, denies the allegations contained in subparagraph (e) of paragraph 6 of the petition.

Denies, generally and specifically, each and every allegation contained in the petition not hereinbefore admitted, qualified or denied.

Wherefore, respondent prays that the Court redetermine the deficiencies herein to be the amounts determined by the Commissioner, viz.: Income tax for the calendar years 1944, 1945 and 1946 in the respective amounts of $40,768.14, $24,588.00 and $38,683.15.

(Signed) Mason B. Leming
Mason B. Leming G.W.B.
Acting Chief Counsel
Bureau of Internal Revenue

Of Counsel:
John D. Kiley
District Counsel

Thomas A. Steele, Jr.
Special Attorney
Bureau of Internal Revenue

[fol. 55] Narration of Testimony of WALTER D. JOHNSON.

My name is Walter D. Johnson and I am presently employed by the Mayflower Distributing Company and was employed there in the early part of 1943 and continuously during the years of 1943, 1944, 1945 and 1946. I am an accountant and was in charge of the bookkeeping and accounting department. I was engaged by Mr. Taran, who was one of the partners of Mayflower Distributing Co.

When I came to work at Mayflower, Mr. Herman Paster was general manager of the business, and I received most of my orders from Mr. Taran, except some that had to do with the sales from Mr. Paster. [fol. 57]

My duties at the Mayflower were the keeping and maintaining of the books and records of Mayflower and making entries therein and the preparation of income tax returns for the partnership. [fol. 57]

I discussed with Mr. Paster the Trust Agreements which were marked in evidence as Exhibits 4(a), 4(b) and 4(c), and Mr. Paster asked me to keep the records of the transactions of the trusts which I did. [fol. 58]

Petitioner's Exhibit 5, shows a balance transferred from previous records on February 1, 1943, to the credit balance of $51,511.82 and carried over from the previous set of books from January 31, 1943. The next entry on this exhibit shows that $30,000.00 was transferred to a

notes payable account entitled H. Paster, S. Walzer trust. [fol. 61]

Exhibit 6 is the ledger account of the Mayflower books entitled—Notes Payable, H. Paster, Sam Walzer Trust. On Exhibit 6 an amount was set up as a trust investment of $30,000.00 to the credit of the trusts. [fol. 64] This is the corresponding entry to the entry which I testified to in relation to Exhibit 5. The entries on Exhibit 6 were made pursuant to instructions of Mr. Taran. I received my instructions regarding the accounting of the books of Mayflower from Mr. Taran. [fol. 66].

"The Witness: Well, when it came time to close the books there was naturally this entry on the books to cover this trust investment and I asked him how I was to make the distribution of the profits for the year ending January 31, 1944, and he indicated to me that each one of the trusts were to get seven percent of the profits." [fol. 67]

A memorandum entitled "Mayflower Distributing Co., Determination of Moneys Due Others, Year February 1, '43—January 31, '44" was prepared by me at the close of the fiscal year ending January 31, 1944, (this was offered in evidence as Exhibit 7, Folio 70), and represents my working papers which I kept concerning the transactions with the trusts and source of the identical figures shown on exhibit 6 as entry of profits between the trusts, fiscal year ended January 31, 1944, before entering the figures on the books from this memorandum I showed it to Mr. Taran. [fol. 69] Mr. Taran gave me instructions as to the manner of computing the profit to the trusts.

On Exhibit 7 is the following memorandum: "In consideration of ten thousand dollars invested in business for each of three trusts, the partnership has agreed to pay seven percent of profits to each of trusts in return

the original investment to remain in business and not subject to being withdrawn without consent of the partnership." [fol. 70 and 71].

A memorandum entitled "Mayflower Distributing Co., Determination of Moneys due others, Fiscal Year February 1, 1944 to January 31, 1945." (this was introduced in evidence as Exhibit 8—Folio 74) and a memorandum entitled "Mayflower Distrbuting Co., Schedule for Determining Percentage Profits to Others based on Income during fiscal year 2-1-45 to 1-31-46" (Folio 72 and 73) (this was introduced as Exhibit 9—Folio 74) were both prepared by me and are in my own handwriting. These computations were prepared upon the instruction of Mr. Taran. These figures were entered on the ledger account, Exhibit 6, and before entering these on the books they were shown to Mr. Taran, who agreed to them, and immediately thereafter I made the entries on the books. [fol. 73 and 74].

Exhibits 7, 8 and 9, being the three computations of profits for each of the three years were prepared by me in the regular course of business. [fol. 75].

During the years of 1944, 1945 and 1946, I kept separate running accounts recording all the transactions that had anything to do with the trusts, and there were no separate sets of books because all the transactions were on the books of the Mayflower Distributing Company, and the information thereon was complete, and I considered these the records of the Mayflower sufficient for trust purposes. [fol. 75]

The three sheets marked Exhibit 10(a), 10(b) and 10 (c) entitled "Herman Paster, Sam Walzer, trustees for Celia Paster", on the first sheet; "Herman Paster, Sam Walzer trustees for Donald Paster", on the second sheet,

and "Herman Paster, Sam Walzer, trustees for Edward Paster", on the third sheet, these are running accounts of these various trusts. [fol. 77].

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[153] Narration of Testimony of HERMAN PASTER.

My name is Herman Paster and I am the petitioner in this case. At the end of 1942 I was employed by the Mayflower Novelty Company and S. H. Taran was my employer. [153] Up to the end of 1942 I received $75.00 a week and twenty percent of the net profits. At the end of that year Mayflower was indebted to me approximately a little over $50,000.00.

The Trust Agreements which have been introduced in evidence bearing my signature were prepared by Attorney Manley Frisch. I told him I wanted to set up a trust for my children and my wife, and I wanted to put $30,000.00 into these trusts, $10,000.00 for Mrs. Paster, $10,000.00 for Donald Paster, and $10,000.00 for Edward Paster. [fol. 155].

I discussed these trusts with my counsel and I understood that in setting up these trusts I will never be able to take out the money placed in trust or any of the trust earnings and it was my intention to separate myself from these funds forever. [fol. 156]. My purpose in setting up these trusts was to secure the future of my wife and children in case anything should happen to me. The trusts were to terminate when each of my children reached the age of twenty-one. [fol. 157] It was my intention that when my oldest son became twenty-one years of age then the trust for my wife would terminate and the proceeds go to her. The trustees of these trusts were Sam Walzer, my brother-in-law, and myself. [fol. 158]

When I set up the trusts I was contemplating on buying some real estate for the trusts. [fol, 159] I did not, however, receive the money that the Mayflower Novelty Company owed me, and after several discussions with Taran he asked that the money the Mayflower owed me be left with them and he made several attractive proposals for leaving the money there, one of which was that the trusts would receive 21% of the profits. [fol. 161]

I told Mr. Taran that I would talk it over with my wife and let him know. After I talked it over with my wife, several days later I agreed to leave the money in there. [fol. 162] At the time I made this arrangement to leave the money in the business for the trusts. the business was in need of money. [fol. 164]

The testimony with reference to this arrangement read as follows:

"Q. Well, do you recall anything alse that you may have had in mind as to plans for the use the trusts might make of this money?

A. Well, it was—I was thinking of investing it in real estate. [fol. 160]

Q. Well, in fact, did you at the end of that year collect the money from the business?

A. No, sir.

Q. How did it come about that you did not collect it from the business?

A. Well, I had several discussions with Mr. Taran and he asked me to leave the money in there, and he made several proposals, attractive proposals, and I decided to leave it there.

Q. So when did you have those conversations with Mr. Taran?

A. I have had them in the early part of January, it was the first week in January 1943.

Q. Well, who started the discussions?

A. Mr. Taran.

Q. What did he say?

A. Well, at that time the Mayflower didn't have that kind of money to pay me out. He was just buying out Mr. Roisner and he proposed to leave the money there, and we were going to share, the trust was going to share a profit of twenty-one percent of the earnings.

Q. Had you told Mr. Taran about the trusts?

A. Yes, I did.

Q. Had you told him that you had assigned the moneys?

A. Yes, sir. [fol. 161]

Q. Continue with the conversation.

A. I am sorry, I did not assign the money at that time, because the trust was not fully developed at that time; I am sorry.

Q. When was this conversation?

A. That was in the early part of January.

Q. Well, you had executed the trusts on the 29th?

A. Yes.

Q. Of December?

A. That is right. But it wasn't fully decided, you know, when I should take the money out from there, see.

Q. Well, continue with the conversation that you had with Mr. Taran.

A. Well, then he asked me to leave the money there and I told him, "I will talk this over with the trustee of the trust, Mr. Walser, and talk it over with Ceil",—that is Mrs. Paster, and I will let him know. And we talked it over and several days later I told him that we agreed to leave the money in there, and then I asked him what my benefits will be from it being there, and leaving the trust there, the money for the trusts, rather, and he told me that I will receive fourteen percent instead of twenty percent, I will have to sacrifice six percent of my previous bonus, and he will also increase my salary from seventy-five dollars to one hundred dollars a week plus a car." [fol. 162]

Mr. Taran also told me that as long as the money will stay with Mayflower the trusts would receive 21% of the profits [fol. 163]

Mr. Taran had not established any channels of credit for borrowing money and that is the reason he was willing to give up twenty-one percent of the profits of the business for the permanent loan of $30,000.00. [fol. 165]

[fol. 416] T. C. Memo. 1956-144

THE TAX COURT OF THE UNITED STATES

HERMAN PASTER, Petitioner, v. COMMISSIONER OF INTERNAL REVENUE, Respondent.

Docket No. 39018. Filed June 20, 1956.

Served June 21, 1956.

Sidney J. Kaplan, Esq., and Claude E. Petersen, Esq., for the petitioner.

J. Marvin Kelley, Esq., for the respondent.

MEMORANDUM FINDINGS OF FACT AND OPINION

TURNER, Judge: Respondent has determined deficiencies in income tax against petitioner for the years 1944, 1945 and 1946 in the respective amounts of $40,768.14, $24,588 and $38,683.15.

The question for decision is whether the partnership profits credited on the partnership books as trust income were the income of the petitioner. A question with respect to a $7,000 adjustment of deductions for miscellaneous expenses for 1946 has been conceded by the petitioner. [fol. 417] Similarly, a $4,800 adjustment to salary for the year 1946 has been conceded by the respondent.

FINDINGS OF FACT

Some of the facts have been stipulated and are found as stipulated.

Petitioner is a resident of St. Paul, Minnesota. He filed his income tax returns for the taxable years here in question with the collector of internal revenue for the district of Minnesota.

For some period not shown but prior to 1937, petitioner had been engaged as a salesman of novelty equipment such as pinball machines, juke boxes and miniature bowling alleys. He decided to go into business for himself and early in 1937 rented a small place in St. Paul, bought some machines in Chicago and had them shipped c.o.d. He borrowed the money to pay for the machines from Samuel Taran, his wife's uncle. Within approximately one month his funds were depleted and he was unable to continue the business. He reported the matter to Taran who took over the business and employed petitioner to run it for him.

Petitioner was to receive as compensation for such services $35 per week and 15 per cent of profits.

The business, sometimes referred to as Mayflower, was first known as Mayflower Novelty Company but after January 31, 1944, used the name Mayflower Distributing Company. Its business was that of buying, selling, distributing and operating coin-operated machines, apparatus and devices. Its books were kept and its returns were filed on the basis of a fiscal year ending January 31.

According to its returns, Mayflower was a partnership from the time Taran took over the business until January 31, 1946, when it was purchased by petitioner. As shown [fol. 418] by the returns filed, the partners were Taran, his nephew J. H. Nilva, and a trust denominated "S. H. Taran, J. H. Nilva Trust." J. H. Nilva was listed on the returns as being in the Navy for each of the years herein. On the return for the year ended January 31, 1944, his share of the profits was reported as $37,266.52. No profits were reported for him for the years ended January 31, 1945 and 1946. For the fiscal year ended January 31, 1944, $67,079.73 was reported as the distributive share for the trust. For the years ended January 31, 1945 and 1946, when no distributive shares were shown for Nilva, the distributive shares of the partnership profits were shown 50 per cent to Taran and 50 per cent to the trust. For the fiscal year 1945, 50 per cent of the ordinary net income reported was shown as $53,978.66. Net long-term gain was also reported, 50 per cent thereof being shown as $198.50. In the return for the fiscal year 1946 a net operating loss of $34,978.51 was reported. Net short-term gain was shown as $89,372.02, net long-term gain as $67,015.37. The net operating loss and the net short- and long-term capital gains were reported as being 50 per cent distri-

butable to Taran and 50 per cent distributable to the trust. When petitioner acquired the business at January 31, 1946, however, all funds standing to the credit of Nilva individually and to the trust were distributed to Taran.

During parts of 1944 and 1945 Taran was incarcerated in a Federal prison at Sandstone, Minnesota. He was an alien and not a citizen of the United States.

Under date of December 29, 1942, petitioner executed three instruments entitled respectively "Herman Paster—Trust Agreement for the Benefit of Celia Paster," "Her- [fol. 419] man Paster—Trust Agreement for the Benefit of Donald Joseph Paster" and "Herman Paster—Trust Agreement for the Benefit of Edward Jacob Paster." In each instrument it was recited that petitioner, called therein "the Donor," has "transferred, assigned, set over and delivered * * * unto himself and Sam Walzer" as trustees "A Ten Thousand ($10,000.00) Dollar interest in the proceeds due Herman Paster as earnings for services rendered to the Mayflower Novelty Company." Celia Paster is petitioner's wife and Donald Joseph and Edward Jacob are his sons.

Except as to the named beneficiaries and the dates for termination of the trusts, the instruments were identical and among other things each instrument recited that the trustees should have full power to sell, buy and manage any property comprising the trust property, "to collect, recover, and receive the income thereof and therefrom," and should not be responsible for any loss or damage which might result from the exercise of judgment or discretion "nor for any moneys or property except such as shall actually and in fact come into their possession" under the instrument; that no part of the income should be used to pay any life insurance premiums on policies

on the life of petitioner; that at least 15 per cent of the income should be distributed annually to the beneficiary and the remainder distributed or retained as corpus in the discretion of the trustees; that the trusts should terminate on November 18, 1960, in the cases of Celia and Donald Joseph, that date being Donald Joseph's twenty-first birthday, and in the case of Edward Jacob on August 22, 1962, which would be his twenty-first birthday; that in the event of death of the beneficiary distributions were to go to issue and there being no issue to heirs at law; that the trustees should "keep and maintain separate [fol. 420] books and records covering the trust estate"; that the trust was irrevocable and should not be capable of modification except as in the instrument specifically authorized and directed; that additions to the trust res might be made by petitioner or others by the execution to that effect by the contributor of an instrument in writing and written acceptance thereof by the trustees; and finally that each trustee should receive $100 per year as compensation for his services. Each instrument also contained provision which for the purposes here may be referred to as spendthrift provisions.

Sam Walzer is petitioner's brother-in-law, being married to petitioner's sister.

On some date not shown, possibly late in 1939, petitioner's compensation for his services to Mayflower had been increased to $75 per week and 20 per cent of the net profits, and at the close of the fiscal year ended January 31, 1943, Mayflower, according to its books, was indebted to him for services rendered in the amount of $51,511.82. In petitioner's drawing account, however, there was a debit balance of $17,443.32, indicating $34,068.50 as the net balance in petitioner's favor per the Mayflower books.

Under date of February 1, 1943, the above $51,511.82 was entered in an account entitled "Note Payable—H. Paster," under the description "Balance transferred from prev book." Of the said $51,511.82, there was no withdrawal from Mayflower of the $30,000 purportedly assigned by petitioner to himself and Walzer as trustees under the above instruments. But also under date of February 1, 1943, a debit of $30,000 was entered in the "Note Payable—H. Paster" account, under the description "trans to Note payable—H Paster, S Walzer trust," and under [fol. 421] the same date an account entitled "Note Payable—H. Paster, Sam Walzer Trust" was credited in the amount of $30,000, as "Amt set up as trust investment."

At the close of the fiscal year ended January 31, 1944, and as "Profits accruing to Trusts fiscal yr end 1/31/44," $51,519.81 was entered as a credit to the above "Note Payable—H. Paster, Sam Walzer Trust" account. The amount so entered had been taken from a memorandum or tabulation prepared by Walter Johnson, Mayflower's accountant and bookkeeper. On this tabulation, which was entitled "Mayflower Distributing Co—Determination of moneys due others—year 2/1/43 - 1/31/44," and after Mayflower's "Combined income," together with some limited breakdown thereof, was shown as $245,332.42, the following appeared:

> In consideration of $10,000.00 invested in business for each of 3 trusts the partnership has agreed to pay 7% of profits to each of trusts in return the original investment to remain in business & not subject to being withdrawn without consent of partnership

7% due Celia Paster Trust		17,173.27
7% due Donald "	"	17,173.27
7% due Eddie "	"	17,173.27
21% totals		51,519.81
14% due H. Paster for services rendered		34,346.54
Total Amt due others		85,866.35

[fol. 422] The above tabulation "Determination of moneys due others" was prepared by Johnson on instructions from Taran and it was shown to Taran before entries were made therefrom in Mayflower's books.

As of February 1, 1943, and pursuant to instructions, presumably from Taran, Johnson had set up on Mayflower's books an account entitled "Note Payable ** M. Roisner" and entered therein a credit of $40,000. Under date June 30, 1943, the account had been closed by an offsetting debit of $40,000.[1]

[1] The identity of Roisner and his relationship to Mayflower or Taran, or his connection with this case, are not clear. In his opening statement, petitioner's counsel had stated that Roisner, "who had theretofore been employed in the business and theretofore had been receiving 15 per cent of the profits, was terminating his relationship with the business," making it possible for Mayflower to apply the 15 per cent previously paid to Roisner to the trusts, and that "the reduction of petitioner's compensation from 20 per cent to 14 per cent supplied the difference between 15 per cent that Roisner had been getting and the 21 per cent that the trusts would receive." In his proposed finding of fact appears the statement that prior to February 1, 1943, Roisner was serving Mayflower in an administrative capacity; that he received a share of the profits of the business, but the evidence does not show what percentage he received. Petitioner and Johnson, the only witnesses called in the trial of this proceeding, either did not know the full story or refrained from giving it. Their testimony ranged from statements that they did not know what Roisner's relationship to the business was or the basis of the payment to him, to Johnson's expressed belief that Roisner "was serving in administrative capacity of some kind" and that he had "the proper connection with factory lines and things that made it worth while to have him connected with the firm" and petitioner's statement that he was an employee, to the further statements by petitioner that though he didn't know what "investment" Roisner had in the business, he did know he received quite a portion of the profits, and that Roisner "was a stranger, and he re-

[fol. 423] Tabulations similar to that indicating "moneys due others" for the fiscal year 1944 were prepared at the close of the fiscal years ended January 31, 1945, and January 31, 1946, from which credit entries to the "Note Payable—H. Paster, Sam Walzer Trust" account were made, the credit under date of January 31, 1945, being shown as "Profits for year end 1/31/45," $33,879.66, and that under date of January 31, 1946, as "Profits for fiscal yr end 1/31/46," $31,680.28. Actually, as shown or reflected by the tabulation, 21 per cent of Mayflower's profits for its fiscal year 1945 was $36,879.66, and not $33,879.66 as credited, the $12,293.22 shown as "7% due Celia Paster, trust" and identical amounts shown as "7% due Donald Paster, trust" and "7% due Eddie Paster, trust" each being reduced by $1,000 described in each instance as "Less hold back to following year." And as reflected by the tabulation for the fiscal year 1946, the amount shown or reflected as 21 per cent of Mayflower's profits for that year was $36,223.26, and not $31,680.28 as actually credited. In truth, however, the amount shown as "Totals" of the three 7 per cent items was neither the $31,680.28 actually credited nor $36,223.26, the correct total for the year, but $39,223.26, the $12,074.42 shown as "7% due Celia Paster, trust" and identical amounts shown as "7% due Donald Paster, trust" and "7% due Eddie Paster, trust" each being increased by $1,000 described in each instance as "Add. Bal due from prev year" or "due from prev yr." In entering the credit in "Note Payable—H. Paster, Sam Walzer Trust" account, however, the aggre-

[1] (Continued)
ceived proportionately, I think, much more than seven per-cent." Furthermore, the significance of the entry closing the account is not known, it being the petitioner's statement that he paid Roisner $7,000 with respect thereto on his acquisition of the Mayflower business in 1946. On his 1946 return, he claimed a deduction of $7,000, under the description "Payment to M. Roisner to remain out of competition in coin machine business for the year 1946."

gate of $39,223.26 so arrived at was reduced by $7,542.98 described as "Cr given H. Paster on Paster Dist Co books for payts to Celia Paster" to arrive at the $31,680.28 actually credited.

[fol. 424] As to petitioner, in the above tabulation for the fiscal year 1945, $24,586.44 was shown as "14% due H. Paster for services rendered," which amount was reduced by $2,000 described as "Less hold back to next year" to arrive at $22,586.44 shown as "Net due to H Paster." $56,466.10 was shown as "Total due to others," and was the total of the $22,586.44 shown as "Net due to H Paster" and the $33,879.66 actually carried into the account "Note Payable—H. Paster, Sam Walzer Trust." In the tabulation for the fiscal year 1946, $24,149.84 was shown as "14% due H. Paster for services rendered," which amount was increased by $2,000 described as "due from prev year" to arrive at $26,149.84. $65,373.10 was shown as "Total pd to others," and was the total of the said $26,149.84 and the above $39,223.26 from which the $31,680.28 actually credited to the trust account was derived.

In the regular course of keeping Mayflower's accounts and in the reporting of its income, the amounts credited to the "Note Payable—H. Paster, Sam Walzer Trust" account and as derived from the above side tabulations were not treated either as in payment for the use of money or as distributions of a percentage of profits based on investment, but as selling expenses. For each of the fiscal years 1945 and 1946, the amounts in question were first entered in the journal in a lump sum described as "H Paster Bonus" and carried from there likewise in a lump sum to a ledger account denominated "Salary & Bonus—H. Paster H Paster, trusts," and then, after

being lumped with the amounts shown as covering petitioner's weekly salary,[2] cleared to profit and loss. For [fol. 425] the fiscal year 1944, there were two journal entries of "Bonus," one as "H. Paster, Bonus" and the other as "H. Paster, Trust, Bonus," the amounts being the same as those shown on the side tabulation "Determination of moneys due others." When carried to the "Salary & Bonus" account in the ledger, however, they were entered in a lump sum, as was done for the fiscal years 1945 and 1946.[3] In the partnership returns, the amounts shown in the "Salary & Bonus—H Paster H Paster, trusts" account, although broken down and shown as salary of petitioner, bonus of petitioner and bonus of H. Paster or Herman Paster "Trusts" or "Trust Funds," were all deducted as selling expenses.

By entry as of January 31, 1944, a debit of $17,188.56, described as "Cr due H Paster for disbursement to C Paster & bonds for Donald Eddie," was entered in the "Note Payable—H. Paster, Sam Walzer Trust" account on Mayflower's books. Penciled notations in proximity to the descriptive matter appear to indicate that $2,118.56 related to "C Paster" and $15,000 to "Donald Eddie." Under date of March 31, 1945, a debit of $16,438.02 was [fol. 426] entered in the said account, with a breakdown in the descriptive statement indicating that it represented payments in various amounts of state and Federal taxes relating to "Edward & Donald" and "Celia." Thereafter, under dates ranging from April 30, 1945, to January 1,

[2] The entries on the ledger sheets placed in evidence began with 1943 and the first entry was $3,400, under date of September 30, and was described "$100.00 wk for 34 wks 2/1/43 thru 9/30/43." Thereafter entries were regularly made as of the end of each month and in amount appeared to represent $100 per week for the weeks which had elapsed since the date of the last preceding entry.

[3] For all three years, and preceding the lump sum entries, there was a descriptive breakdown on the "Salary & Bonus" account as between "Bonus—H Paster" and "trusts," the amounts of such breakdowns being the same as shown on the above side tabulations.

1946, five debit entries amounting in the aggregate to $2,717.76 were made in the said account, four of which, according to descriptive wording, related to 1944 and 1945 state tax and income tax "Celia Paster," whereas the fifth entry, in the amount of $68.52, was described as "Ins premium N W Natl Life Donald P Paster." Under date of January 31, 1946, the said account on Mayflower's books was closed by a debit entry of $110,735,41, under the description "Trans to H Paster draw in exchange for note."

No books were ever set up or maintained for the three trusts purportedly created by petitioner under the instruments above. Johnson did maintain in pencil and on ruled yellow worksheet paper what he has denominated as a running account for each purported trust. There was one sheet for each such trust and the sheets were kept by Johnson in his desk. According to these sheets, and aside from original credits of $10,000 each, the aggregate of credits up to and including January 31, 1946, was $124,622.73, or $41,540.91 to each sheet. On the "Herman Paster—Sam Walzer trustees for Celia Paster" sheet and in a column headed "deductions" is an undated entry, but presumably made prior to January 31, 1944, of $2,188.56 described as "Payt on note—stock pool advance." There were no entries under "deductions" for the fiscal year 1945. A further entry described as "Payt on note stock pool advance," in the amount of $7,542.98, was made under date of January 31, 1946. Under dates ranging from March 14, 1945, to "Dec. 45," seven other entries were made in [fol. 427] the "deductions" column, amounting in the aggregate to $8,605.32, which entries purport to cover payments of taxes. On the sheets denominated "Herman Paster—Sam Walzer trustees for Donald Paster" and "Herman Paster—Sam Walzer trustees for Edward Pas-

ter" and in columns headed "deductions," $7,500 was shown for the fiscal year 1944 on each sheet, that on the Donald Paster sheet being described as "Withdrawn by H. P. for bonds" and that on the Edward Paster sheet being described as "Withdrawals by H. P. for bonds & Real Estate." No amounts were entered as "deductions" for the fiscal year 1945. For the fiscal year 1946, four entries, in the aggregate amount of $5,245,97, are shown on each sheet and described as 1944 Federal and state fiduciary and individual tax. On the Donald Paster sheet an additional amount of $68.52, described as "N. W. Natl. Life—ins prem.," was entered under date of "Oct. 45."

In addition to the above and separated by a red line from the columns from which the entries above were recited, each sheet carries a column headed "other trust deductions." On the Celia Paster sheet, under dates ranging from April 1944 to July 31, 1944, there were seven entries, amounting in the aggregate to $8,605.32, and for the fiscal year 1946, three items amounting to $1,109.17. The largest single item was $5,382.16, described as "Payt on note—Stock pool advance." According to descriptive wording, the other nine items purported to cover such matters as tax, hospital insurance, "Mrs. H Paster," "Mrs Paster Rwy ticket," and deposits "C Paster ch ing a/c." On the Donald Paster sheet, the "other trust deductions" entries were $116.44 for the fiscal year 1944, $330.25 for the fiscal year 1945 and $264.32 for the fiscal year 1946, consisting in all of seven entries, all of which purportedly [fol. 428] were for insurance premiums paid to "N. W. Natl Life." On the Edward Paster sheet, in the column "other trust deductions," two entries for the fiscal year 1945, in the aggregate amount of $257.72, and two entries, amounting in the aggregate to the same amount, for the fiscal year 1946 were shown, and according to the descrip-

tive wording, were for insurance premiums paid to "N. W. Natl Life."

According to explanatory symbols, the items entered, as noted above, in the column headed "other trust deductions" represented amounts paid by Mayflower Distributing Company, Paster Distributing Company and H. Paster personally. Although they appear as indicated on the so-called trust accounts and were possibly provided by or at the instigation of petitioner, they were not taken into account in arriving at the $110,735.41, the entry closing out the "Note Payable—H. Paster, Sam Walzer Trust" account on Mayflower's books, as having been transferred to petitioner "in exchange for note."

The entries on the three yellow sheets purport to extend through October 31, 1947. The only amounts shown as credits on the Celia Paster sheet after January 31, 1946, were in three entries, two in February and one in July of 1946, and four entries one each in February, March, July and August of 1947, the 1946 entries amounting in the aggregate to $262.50 and those for 1947 to $275. These items were all described as interest on bonds or interest on government bonds. The only other items shown on the Celia Paster sheet dated after January 31, 1946, were in the "other trust deductions" column, and consisted of four items in 1946, amounting in the aggregate to $8,238.95, seven in 1947, amounting to $2,985.87. The largest single item, as was true of earlier years, was described as "Cr for cash advanced on Stock Pool," and was $7,542.98. [fol. 429] The other items, with one exception, were described as payment of Federal and state taxes. The one exception was dated "June 1947" and described as "R E tax 1952 Pinehurst 1st half." On the Donald Paster sheet, only one amount, $762.91, described as "Refund on '46 tax," was shown as an addition to the purported trust fund

after January 31, 1946. Seven items amounting in the aggregate to $2,892.91, from April to October, 1946, and six items amounting in the aggregate to $4,648.08, from January to October, 1947, were entered in the column "other trust deductions," and according to descriptive wording, represented payments of state and Federal personal and fiduciary tax or insurance premiums. On the Edward Paster sheet, there was similarly only one amount, $762.91, described as "refund on 46 Fed tax," entered after January 31, 1946, as an addition to the purported trust fund. Six items, amounting in the aggregate to $2,817.97, ranging in dates from January to September, 1946, and five items, amounting in the aggregate to $4,570.35, under dates from January to October, 1947, were entered in the column "other trust deductions," and as in the case of Donald Paster, were described as payments for state and Federal fiduciary and personal taxes and insurance premiums.

On all three sheets the items entered under dates subsequent to January 31, 1946, in the columns headed "other trust deductions," were by symbols shown as having been paid by Mayflower Distributing Company, Paster Distributing Company, Paster Enterprises and H. Paster personally.* There were no entries on any of the sheets de- [fol. 430] signed to show any payments or additions to the purported trusts after January 31, 1946, of profits payments or distributions by Mayflower, its successor, or successors.

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*From petitioner's individual income tax return for 1946, it would appear that Paster Enterprises was an individual enterprise of petitioner, although it was Johnson's testimony that it represented "some real estate holdings of Mr. Paster and Mrs. Paster." As to Paster Distributing Company, there is some indication of record that it was the name applied to the business of Mayflower after it was acquired by petitioner. On some undisclosed date or dates after petitioner's acquisition, the various branches of the business appear to have been separately incorporated, each taking the name Paster Distributing Co., Inc.

Johnson was a graduate in accounting from the School of Business Administration of the University of Minnesota, and except for a portion of his duties in a prior employment, his work and experience during his business life had been in the accounting field.

During the fiscal year ended January 31, 1944, Mayflower in the course of or in connection with its business obtained a loan or loans amounting to $35,000 from a St. Paul bank, and according to its return of income for that year, incurred interest thereon of $1,166.63. Also according to its return, it had interest expense for that year of $2,635.36 to Coin Machine Acceptance Corporation, Chicago, Illinois; $119.59 to Northwestern National Bank, Minneapolis; $226.53 to Central Bank & Trust Company, Des Moines; and $634.72 to Broad Street Trust Company, Philadelphia, Pennsylvania, bringing total interest expense reported to $4,982.13. Also according to its return of income for the fiscal year 1944, it incurred finance fees of $22,171.65 to Utility Finance Company. For the fiscal year ended January 31, 1945, it incurred, according to its return of income, [fol. 431] interest of $250 to Central National Bank & Trust Company, Des Moines, and $1,215.87 to Northwestern National Bank, Minneapolis, or a total of $1,465.87. It also reported finance fees to Utility Finance Company of $22,999.22. The Utility Finance Company was owned by or was the individual enterprise of Taran. On its return for its fiscal year ended January 31, 1946, Mayflower reported interest payments of $12,864.45 and finance fees of $6,946.44.

The profits of Mayflower credited on its books to the "Note Payable—H. Paster, Sam Walner Trust" account for each of the fiscal years ended January 31, 1944, 1945 and 1946, were income to petitioner and in so far as the side tabulations of moneys or percentages of profits "due others" for each of those years or the entries made on

Mayflower's books or the three sheets maintained by Johnson tend or purport to show otherwise, they are shams and do not reflect the facts.

OPINION

The question is whether $51,519.81 for 1944, $33,879.66 for 1945 and $39,223.26 for 1946 was the income of petitioner, and not the income of trusts for Celia, Donald and Edward Paster, as shown by the tabulations of moneys or profits "due others" for Mayflower's fiscal years 1944, 1945 and 1946.

It is the claim of the petitioner that he made bona fide gifts of $10,000 each to valid and subsisting trusts for his wife and each of two sons; that through oral agreements with Taran, entered into in January of 1943, the corpus of each of the three trusts was left with Mayflower and for the use of such trust funds the trusts were entitled to receive, and did receive, 21 per cent of the profits of May- [fol. 432] flower for each of the fiscal years 1944, 1945 and 1946. It is the position of the respondent that the arrangement or agreement with Taran was nothing more than a scheme to split the earnings of petitioner for income tax purposes, and, in that respect, was a subterfuge and a sham and the amounts in question represented earnings of petitioner, and are taxable to him.

To maintain his position, petitioner relies on his own testimony, the testimony of Johnson and certain documentary evidence which for the most part consists of transcriptions from Mayflower's books of account, which were kept by Johnson, and various Federal income and tax returns prepared by him. It does appear that the three trust instruments, plus certain of the bookkeeping entries and accounting records, were designed and purport to

show and indicate the ownership by the trusts of the $30,000 purportedly granted to them but retained and used in Mayflower's business and in consideration of which the payment of the indicated percentage of the profits was to be made to the trusts as petitioner claims. The contention is also supported by various assertions and statements in the testimony of both petitioner and Johnson. From other records and other portions of the testimony of petitioner and Johnson, however, we are convinced that determinative facts require a conclusion contrary to that for which petitioner contends.

According to petitioner's testimony, the arrangement between him and Taran for the retention and use by Mayflower of $30,000 of the moneys due him for services rendered and which he purportedly had assigned to the trusts was orally agreed upon in January of 1943. The agreement was never reduced to writing and there were no witnesses to the discussion, although petitioner did testify [fol. 433] that he talked the matter over with Celia, his wife, and with Sam Walser, his co-trustee. Taran was not a citizen of the United States, and as pictured by petitioner did not, to say the least, have a wholesome reputation. It was petitioner's testimony also that he personally had had difficulties with Taran on prior occasions and had been discharged several times from his employment with Mayflower, and at the time of the purported agreement was concerned lest he be discharged again. On the basis, however, of an oral promise from Taran that even if petitioner should be discharged the participation of the trusts in Mayflower's profits should continue, he asserts that he proceeded to commit to Taran's use and control $30,000, not of his money but money in respect of which, according to his claim and testimony herein, he and Walser then stood in a fiduciary capacity. He admitted that Mayflower

was engaged in a hazardous business and might be affected adversely by legislation since "pinball" companies were not popular with the Legislature. And to make the story even more bizarre and incongruous, it would appear from the memorandum on the tabulation "Determination of moneys due other 2/1/43 - 1/31/44," upon which petitioner relies, that under the agreement with Taran he and Walzer could not withdraw the said $30,000 from Mayflower without its, namely, Taran's, consent. In contrast with the stated restriction on the withdrawal of the $30,000 of purported trust funds and anent petitioner's testimony of Mayflower's difficulties in procuring the cash required for its operations and of his individual difficulties and differences with Taran, it is to be noted from Mayflower's books of account that petitioner, by January 31, 1944, had been [fol. 434] permitted to overdraw his personal drawing account by at least $64,542.92,* as against a credit balance of only $21,511.82 in the "Note Payable—H. Paster" account. The overdrawing of his drawing account was apparently the usual thing with petitioner, since $17,443.32 of the total at January 31, 1944, had been from the fiscal year 1943.

And though the business of Mayflower was growing, and such being the circumstances it would be only reasonable to conclude that his responsibilities as its manager were becoming correspondingly greater, it is to be noted that under the claimed agreement petitioner was consenting to a reduction in his compensation, namely, a reduc-

* $64,542.92 is a computed balance as reflected by one ledger sheet of petitioner's drawing account, placed in evidence. The account "Note Payable—H. Paster," however, shows a charge under date of January 31, 1944, of $69,686.92 as a transferred debit "from drawing a/c." Under the same date petitioner's "Note Payable" account was credited with $17,188.86 as having been expended by petitioner for trust beneficiaries. An offsetting charge of $17,188.86 was entered under the same date in the "Note Payable—H. Paster, Sam Walzer Trust" account.

tion of his bonus from 20 to 14 per cent of Mayflower's profits. It is argued that this reduction was made up or accounted for by an increase in his weekly recompense from $75 to $100 per week, and in addition he was to receive the use of an automobile. The facts show, however, that the bonus had become substantially the major part of petitioner's compensation and there is no showing that a $25 increase in his weekly stipend, together with the use of an automobile, would be in any way comparable to the [fol. 435] 6 per cent of Mayflower's profits which he was agreeing to relinquish. In any event, the news of the arrangement does not appear to have been currently transmitted to Johnson, or Johnson was quite lax or greatly behind in his bookkeeping, since the first entry on Mayflower's books, at least so far as the record shows, relating to the weekly salary as increased was not made until September 30, when $3,400 purportedly representing $100 per week from February 1 to the end of September was entered in the ledger account "Salary & Bonus—H. Paster H. Paster, trusts." This entry apparently was from a journal entry of the same purport and under the same date.

Although he was aware of the trust instruments, having signed them as a witness, Johnson's first knowledge, so far as appears, of any details of the purported profit sharing arrangement by the trusts came at the end of Mayflower's fiscal year ended January 31, 1944, when, according to his testimony, he was instructed by Taran to prepare a statement showing the distribution of Mayflower's profits for the year and was told that each trust was to receive 7 per cent and petitioner 14 per cent of Mayflower's profits. Pursuant to those instructions, he made up the side tabulation "Determination of moneys due others" and on that tabulation, after showing amounts as

the net income of the St. Paul, Des Moines and Buffalo branches of Mayflower's operation and allowing for amounts denominated "Salary—S. H. Taran," entered as belonging to the trusts and to Paster the above indicated percentages. From this tabulation he made appropriate journal entries from which he carried the percentages so computed to an account denominated "Note Payable—H. Paster" and to an account then set up, or which had [fol. 436] been set up, as "Note Payable—H. Paster, Sam Walzer Trust." In passing it may be observed that no notes were shown as ever having been issued and although Johnson expressed his understanding to be that notes were to be issued, there is no other indication of record that there was ever any intention that notes should be issued.*

More revealing and indicative of the true situation, we think, are various other entries and records made by Johnson in the regular course of keeping Mayflower's accounts and preparing its partnership returns. On Mayflower's returns of income for the years ending January 31, 1944, 1945 and 1946, the so-called bonus to the trusts was listed and deducted as "Selling Expenses" along with the amounts shown as petitioner's salary and bonus whereas finance fees and interest on loans were deducted as "Administrative Expenses." This treatment on the returns of the amounts in question appears to be a follow through of the original entries made by Johnson in Mayflower's journal. The entries for the fiscal year 1944 made immediately following his instructions from Taran did separate

* One of the exhibits placed in the record by petitioner was a copy of the ledger account relating to the mystery man, H. Reisner. That account likewise was set up under the description "Note Payable" but, as in the above instances, there is no indication or showing that any notes were issued or intended to be issued. In fact, such information as does appear of record would cast a grave doubt as to whether the $60,000 was ever paid by Mayflower, even though the account was closed by a credit entry some four months after the original entry was made.

the so-called "H. Paster, Trust, Bonus" from the H. Paster [fol. 437] Bonus" but for the fiscal years 1945 and 1946 the journal entries show only one sum with the explanatory wording "H. Paster Bonus" and it was only in making the entries in the ledger accounts "Note Payable—H. Paster" and "Note Payable—H. Paster, Sam Walzer Trust" that the amount so entered in the journal as "H. Paster Bonus" was divided as between petitioner individually and the trusts. Regardless of that breakdown in the two so-called "Note Payable" accounts, however, the entire amount in the regular course of keeping Mayflower's books was carried through the "Salary & Bonus—H. Paster H Paster trusts" account, into profit and loss and as already noted into the partnership returns as "Selling Expenses."

It was Johnson's testimony that the purported trust bonus was listed in the partnership returns as "Selling Expenses" because it was "in the sales expense category in the book of accounts." To the question on direct examination "Did you intend to indicate by that that that profit sharing bonus was being paid to anybody for doing any selling," Johnson answered "No." The only explanation offered as to why he considered the share of the profits credited to the trusts as a bonus and entered it on the returns as selling expenses, when purportedly it was compensation for the use of money, was that he "probably * * * didn't think of any better name to call it at that time," and though it was the largest single item listed under "Selling Expenses" his further statement was that "It evidently was made in the wrong part of the books, * * * but for simplicity and for ease of obtaining information on the account, when it was necessary, it was placed together with Mr. Paster's account in the selling expenses account."

[fol. 438] We fail to see how the grouping of what was a purported share of profits paid for the use of money with petitioner's bonus and salary as a selling expense was a more convenient and simple way of handling the account as Johnson represented, unless it was in truth and in fact compensation due petitioner for services rendered and the side trust account was designed under an arrangement by petitioner with Taran to give the so-called trust bonus the appearance of being other than it was. For while it does appear that Johnson was neither a certified public accountant nor a public accountant, the record shows that he was a graduate in accounting from the School of Business Administration of the University of Minnesota, and except for a portion of his duties in a prior employment his work and experience during his business life had been in the accounting field. And though it was in response to a leading question from petitioner's counsel Johnson agreed that he did "know the principles of accounting and bookkeeping." From a study of the record, including the various returns prepared by Johnson and the portions of books of account kept by him, we are not convinced that Johnson would classify liabilities incurred, as selling expenses unless for the purpose of properly reflecting Mayflower's operations he actually regarded them as such.

We are also satisfied on the evidence that petitioner's dominion over and use of the balance claimed as the trusts' portion of Mayflower's earnings for the years herein are inconsistent with a status of trustee with respect thereto and with his claims herein. The petitioner admittedly became the owner of the Mayflower business not later than January 31, [fol. 439] 1946,[1] at

[1] Mayflower's partnership return for the fiscal year ended January 31, 1946, shows on schedules attached that the Des Moines Branch was sold by Mayflower to the "Paster Distributing Company" on September 19, 1945, and the schedules relating to the Buffalo operation show a cutoff date of August 4, 1945.

which time, according to the "Note Payable—H. Paster, Sam Walzer Trust" account, the balance owing by Mayflower to the trusts was $110,735.41. No part of this amount was paid by Mayflower and the account was closed by a debit of $110,735.41 indicating assumption of a liability in that amount by petitioner. Actually the closing entry on Mayflower's books indicates that Paster had issued his note covering the liability, but there again there is no indication or claim that he did issue such a note or that it was ever intended that he would.

In the course of his testimony petitioner was put through a series of questions patently designed to indicate that "not a cent" of the withdrawals of the "trust shares" of profits of Mayflower were used for living expenses of petitioner's wife or children or for petitioner's own personal use, and that the setting up of the trusts was real and genuine and not a sham transaction, to which questions petitioner was able to give the desired answer merely by saying "No sir." Later in his testimony, however, and after explaining some of the withdrawals which were entered in the Mayflower accounts and on the sheets maintained by Johnson for the trusts it was petitioner's testimony "and I also drew some money for a home." We were left without explanation as to the date of the withdrawal of the "money for a home," the amount thereof, or the identity of the property. But, whatever may be the truth as to the purchasing of a family home and the source of [fol. 440] the funds used therefor petitioner admits that after his acquisition of Mayflower the trusts had no participation in the profits of the business, it being his testimony that he assumed and satisfied the said liability "to the trusts" by turning "over two apartment buildings, and by purchasing bonds for them." We are not advised, however, as to the date or dates of the claimed transfers or purchases, and beyond the as-

sertion that the down payment on the two apartments, identified by him as 2171 and 2175 Grand, amounted to $50,000 and the total price to be paid was $150,000, we are left in the dark as to the value of his equity in the properties at the time of the claimed transfer or whether such value was in any way comparable to the amount which it is claimed he owed to himself and Walzer as trustees. We do know, however, that on his income tax return for the calendar year 1946, the properties at 2171 and 2175 Grand, presumably standing in the name of Paster Enterprises, were shown as belonging to petitioner as late as December 31, 1946, that in the said return he reported as his income substantial rentals from the properties and in arriving at his net income deducted an allowance for depreciation on the buildings for the calendar year 1946. Further, there is no claim or contention that any of the rentals for 1946 were ever assigned to the trusts or regarded as belonging to them. We also know that up to October 6, 1947, no entries had been made on the sheets maintained by Johnson for the purported trusts which would in any way reflect the payment by petitioner of the $110,735.41 claimed to have been owed to the trusts, the receipt by the trusts of any payments for the use thereof, or the purchase of any bonds or the transfer of the two apartment buildings in satisfaction of the liability which he says he assumed. [fol. 441] In short, even if we should take petitioner's testimony at its face, it would appear that he or his business was making free use for an indefinite period or at least through October 6, 1947, of the $110,735.41 in respect of which he and Walzer are claimed to have been trustees.

Johnson in his testimony attempted corroboration of petitioner's claim that he satisfied the claimed "liability" to the trusts by transfers of real estate. In addition to the apartment houses at 2171 and 2175 Grand,

Johnson also included the transfer of a residence[6] at 1752 Pinehurst Street. Much better corroboration, we think, would have been the record proof of such transfers which would have included the dates thereof as well as the description of the properties transferred, particularly when it is noted that Johnson had very little, if any, personal or direct knowledge in the matter. Though he had made no entries either on Mayflower's books of account or the sheets maintained for the trusts to that effect, it was his testimony on cross-examination that the three properties had been purchased by petitioner with moneys which belonged to the trusts. On redirect and in response to leading questions it was his testimony that the properties were purchased with Paster's personal funds. Subsequently, in response to questions by the Court he attributed his only knowledge of the transactions to [fol. 442] what he had been told by Frisch, who was described as a St. Paul attorney and as having drawn up the trust instruments for petitioner.

As supporting his claim petitioner testified that the trust instruments were drawn by a lawyer named Frisch and gave a version of what Frisch told him as to the force and effect of the things done. And though the testimony so given was particularly self-serving, Frisch was not called in corroboration even though he was purportedly practicing law in St. Paul, the city where the trial herein took place. Similarly, Sam Walzer was not called to testify. Walzer was said to have accepted and assumed the duties and responsibilities of co-trustee with petitioner and according to Johnson lived in Minneapolis, the twin city of St. Paul. The failure of Walzer to

[6] Presumably, 1752 Pinehurst was the Paster family home since that was the address given on the 1944, 1945 and 1946 income tax returns of petitioner, of Celia, his wife, and of his two sons, Edward and Donald, and apparently they were living there at least as early as March 15, 1945, since that was the date on which petitioner's individual income tax return for 1944 was filed. As to whether this was the home for which he "drew some money" from the "trust shares" of Mayflower profits the record is silent.

testify appears to be of particular significance when note is taken of petitioner's delay, if not failure, in accounting to himself and Walzer for the funds said to have been owing by Mayflower to the trusts at January 31, 1946, when, according to petitioner, he acquired the Mayflower business and personally assumed the liability. Taran likewise was a key figure in the purported transactions and dealings but did not testify.

We listened attentively to both petitioner and Johnson in the course of their testimony and we observed them throughout. We have since examined and re-examined the transcript and the other evidence of record, and taking into account the record as a whole, we are satisfied and have found as a fact that in so far as the side tabulations of moneys or percentages of profits "due others" for the fiscal years ended January 31, 1944, 1945 and 1946, the entries made on the Mayflower books and the sheets maintained by Johnson or other records relied on herein tend or purport to show that the amounts [Vol. 443] in question were the income of the trusts and not the income of petitioner, they were shams and did not reflect the truth.

Whether petitioner did or may have created or established valid and subsisting trusts for the benefit of his wife and two sons and the trusts did or may have at some time become the owners in trust of the moneys in question or of property transferred in lieu thereof, we do not find it necessary to decide, since on the record we are satisfied that the moneys in question were the income of petitioner, whatever may have been its disposition thereafter. Petitioner's contention is accordingly rejected. Due, however, to concessions made by each of the parties, a recomputation of the deficiencies is required.

Decision will be entered under Rule 50.

[fol. 450] THE TAX COURT OF THE UNITED STATES
Washington

Served— Aug. 24-56
Entered—Aug. 22-56

DECISION

Pursuant to the Memorandum Findings of Fact and Opinion of the Court filed June 20, 1956, the parties on August 17, 1956, having filed an agreed computation of the tax involved, it is

ORDERED AND DECIDED: That there are deficiencies in income tax for the taxable years 1944, 1945 and 1946 in the respective amounts of $40,766.14, $24,588 and $34,637.66.

Enter:
Entered Aug 22 1956
(Signed) BOLAN J. TURNER
Judge.

[fol. 452] IN THE UNITED STATES COURT OF APPEALS
For the Eighth Circuit

Filed in Tax Court
November 16, 1956

Herman Paster, Petitioner,

vs.

Commissioner of Internal Revenue, Respondent.

Docket No. 39018—T. C. Memo 1956—144

PETITION FOR REVIEW

Herman Paster, appellant in this case (petitioner below), by his attorney, Maurice Weinstein, hereby files

his petition for review by the United States Court of Appeals for the Eighth Circuit of a decision of the Tax Court of the United States rendered and entered on August 22, 1956, in the cause numbered 39018 on the docket of the Tax Court of the United States, T. C. Memo 1956—164, which decision found a deficiency against the petitioner, Herman Paster, in the sum of $40,762.14 for the year 1944, $24,958.09 for the year 1945, and $24,627.69 for the year of 1946.

The years involved in this petition are the calendar years ending December 31, 1944, 1945 and 1946.

The question involved in this appeal is whether certain income of "Herman Paster Trust for the benefit of Celia Paster", "Herman Paster Trust for the benefit of Donald Joseph Paster," and "Herman Paster Trust for the benefit of Edward Jacob Paster," constitutes income of the trusts or that of the petitioner.

Under date of December 29, 1943, the petitioner, Herman Paster executed three trusts—"Herman Paster Trust for the benefit of Celia Paster," "Herman Paster Trust for the benefit of Donald Joseph Paster," and "Herman Paster Trust for the benefit of Edward Jacob Paster," and that simultaneously therewith assigned to each of said trusts the sum of $10,000.00 owing to the petitioner by the Mayflower Distributing Company.

That the Mayflower Distributing Company agreed in consideration of said Trusts permitting said funds to remain with the said company that it would pay to the said Trusts a sum equivalent to seven (7) per cent of the profits of the Mayflower Distributing Company.

That pursuant to such arrangement the Mayflower Distributing Company did pay said Trusts the percentage

of profit as agreed, and that said Trusts filed income tax returns and reported said income and paid a tax thereon.

That the Tax Court held that the income paid to the Trusts by the Mayflower Distributing Company was taxable income to the petitioner, which is the basis of the additional tax involved in this appeal.

That the appellant for the years 1944, 1945 and 1946, was and still is a resident of the City of St. Paul, State of Minnesota, and filed his income tax returns for the years 1944, 1945, and 1946, with the Collector of Internal Revenue for the District of Minnesota, at St. Paul, Minnesota, whose office is located within the jurisdiction of the United States Court of Appeals for the Eighth Circuit.

This petition for review is filed pursuant to the provisions of Section 7482 of the Internal Revenue Code of 1954.

Dated at Milwaukee, Wisconsin, this 14th day of November, 1956.

[redacted]
Attorney for Petitioner
633 N. Second Street
Milwaukee 3, Wisconsin



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IN THE

Supreme Court of the United States

OCTOBER TERM, 1956.

No. 460

HERMAN PASTER,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

DAVID PREVIANT
212 W. Wisconsin Avenue
Milwaukee 3, Wisconsin

MAURICE WEINSTEIN
623 N. Second Street
Milwaukee 3, Wisconsin

Attorneys for Petitioner.

The Scheffer Press, Inc., 118 South Clinton Street, Chicago, Illinois

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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1956.

No.

HERMAN PASTER,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

Petitioner prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Eighth Circuit, entered in the above entitled case on June 21, 1957.

CITATION TO OPINIONS BELOW.

The opinion and findings of fact of the Tax Court of the United States in Docket No. 38018 were filed on June 20, 1956, and the decision was rendered on August 22, 1956, and reported as 56144 T. C. Memo. The opinion of the Court of Appeals for the Eighth Circuit, printed as Appendix A hereto, is reported at 245 F. 2d 281.

JURISDICTION.

The judgment of the Court of Appeals was entered on June 21, 1957, and the jurisdiction of this Court is invoked under 28 U.S.C. Sec. 1254(1).

QUESTION PRESENTED.

The question presented here is whether the profits paid to the Trusts by the Mayflower Distributing Company are income taxable to the Trusts or whether such profits are income taxable to the Petitioner.

STATUTE INVOLVED.

Sec. 22, Internal Revenue Code 1939:

GROSS INCOME.

(a) *General definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service (including personal service as an officer or employee of a State, or any political subdivision thereof, or any agency or instrumentality of any one or more of the foregoing), of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. In the case of Presidents of the United States and judges of courts of the United States taking office after June 6, 1932, the compensation received as such shall be included in gross income; and all Acts fixing the compensation of such Presidents and judges are hereby amended accordingly. In the case of judges of courts of the United States who took office on or before June 6, 1932, the compensation received as such shall be included in gross income.

STATEMENT OF THE CASE.

The petitioner from 1937 to January 31, 1946, (R. 17-19) was employed by the Mayflower Distributing Company, a partnership, and was compensated by a salary plus a percentage of the profits. The petitioner at no time during this period had any proprietary interest in, or control of, the partnership.

On December 29, 1942, (R. 19) the petitioner executed three separate irrevocable trusts, for the benefit of his wife and two children, respectively, which trusts provided (Exhibits 4a, 4b, 4c):

> "8. This trust shall remain in force and in effect until November 18, 1960, at which time the trust shall terminate and all funds, both principal and accrued income, then in the hands of the trustees shall be paid over and delivered to the beneficiary."

Simultaneously with the creation of the trusts the petitioner irrevocably transferred to each of the Trusts Ten Thousand Dollars ($10,000.00) out of the moneys due him from the Mayflower Distributing Company. (R. 19) These sums were transferred to the Trusts on the books of the Mayflower Distributing Company as of January 31, 1943, at which time Mayflower Distributing Company was indebted to the petitioner in the sum of $51,511.82 (Exhibit 5, Ledger Acct. Mayflower). (R. 21)

In January of 1943, subsequent to the creation of the three Trusts, the petitioner, as Trustee, on behalf of the Trusts, entered into an agreement with the Mayflower Distribution Company which provided that the initial trust corpus, an aggregate of $30,000.00, (R. 14, 32) would demain in the Mayflower Distributing Company as working capital and would not be withdrawn by the Trusts without the consent of the company. In consideration for the Trusts thus investing the $30,000.00, the company agreed to pay each Trust 7% of its annual profit. (R. 14)

In compliance with this agreement the Trusts received their share of profits from the Mayflower Distributing Company for the years ending January 31, 1944, 1945 and 1946. (R. 21, 22, 23)

The three Trusts in question filed income tax returns for the years 1944, 1945 and 1946, and each Trust reported and paid a tax upon its share of profits of the Mayflower Distributing Company.

The respondent here determined that the profit which Mayflower Distributing Company paid to the Trusts, which the Trusts reported and paid a tax thereon, was not income of the Trusts but was income of the petitioner and assessed a tax for said income against the petitioner.

The Tax Court approved this determination and held that the profits paid to the Trusts by Mayflower was income to the petitioner and taxable to him, from which decision the petitioner appealed. The decision of the Tax Court was affirmed by the Court of Appeals, which decision is sought to be reviewed here.

REASONS FOR GRANTING WRIT.

I. The decision here is in direct conflict with, and a misapplication of the decisions of the Supreme Court in:

(A) *Helvering* v. *Clifford*, 309 U.S. 331, 60 S. Ct. 554.

(B) *Blair* v. *Commissioner*, 300 U.S. 5.

(A) The decision in the instant case squarely conflicts with the decision in *Helvering* v. *Clifford*, *supra*, which established the principle that the income of a trust is taxable to the grantor, only where the grantor remains the owner of the trust corpus after the creation of the trust.

The Supreme Court in the *Clifford* case concluded that the grantor remained the owner of the corpus of the trust after its creation, stating (Pages 556 and 557):

"In this case we cannot conclude as a matter of law that respondent ceased to be the owner of the corpus after the trust was created. Rather, the short duration of the trust, the fact that the wife was the beneficiary, and the retention of control over the corpus by respondent all lead irresistibly to the conclusion that respondent continued to be the owner for purposes of § 22(a)." * * *

But when the benefits flowing to him indirectly through the wife are added to the legal rights he retained, the aggregate may be said to be a fair equivalent of what he previously had. * * * In those circumstances the all-important factor might be retention by him of control over the principal. With that control in his hands he would keep direct command over all that he needed to remain in substantially the same financial situation as before. * * * Thus, where, as in this case, the benefits directly or indirectly retained blend so imperceptibly with the normal concepts of full ownership, we cannot say that the triers of fact committed reversible error when they found that the husband was the owner of the corpus for the purposes of Section 22(a)."

In the *Clifford* case the tax was assessed against the grantor by virtue of the existence of three elements considered in the aggregate:

(a) the short duration of the trust;

(b) the fact that the wife was the beneficiary; and

(c) the fact that the grantor retained control over the corpus.

A decisive and essential factor was the fact that the grantor in the *Clifford* case retained extensive *legal rights* in the corpus of the trust, consisting of the right to revestment of and control over the corpus and distribution of the income. In the words of the Court, " : . . when

the benefits flowing to him indirectly through the wife are added to the legal rights he retained, the aggregate may be said to be a fair equivalent of what he previously had . . . ".

The grantor, Herman Paster, irrevocably transferred the corpus to the trusts, without right to revestment and without right to any income presently or in the future. (Exhibits 4a, 4b, 4c).

Since in the instant case the petitioner retained no legal ownership in the corpus and no right to control the distribution of income, it is obvious that the Court of Appeals in the instant case did not follow the principle in the *Clifford* case.

(B) In *Blair* v. *Commissioner, supra,* the petitioner, Edward Blair, was the beneficiary of a trust created by his father, under the provisions of which he was entitled to receive one-half of the income. The petitioner assigned to his daughter a portion of the beneficial interest in the trust. The Commissioner maintained that the assignment was ineffective and that the income from the assigned interest was taxable to the assignor. Both the Tax Court and the Court of Appeals affirmed the Commissioner's position.

The Supreme Court reversed and held that the assignment was valid and the income was taxable to the assignee and not to the assignor. The Supreme Court held that the decisions in *Lucas* v. *Earl,* 281 U.S. 111, and *Burnet* v. *Leininger,* 285 U.S. 136, upon which the Court of Appeals relied, were not in point or controlling and stated at page 333:

> "In the instant case, the tax is upon income as to which, in the general application of the revenue acts, the tax liability attaches to ownership. (Citing cases) • • •"

The Court stated further (page 333):

> "The one who is to receive the income as the owner of the beneficial interest is to pay the tax. If under the law governing the trust the beneficial interest is assignable, and if it has been assigned without reservation, the assignee thus becomes the beneficiary and is entitled to rights and remedies accordingly. We find nothing in the revenue acts which denies him that status."

In the *Blair* case the income in issue came from the beneficiary's interest in the trust. Analogously, in the instant case the income in issue derived from the funds irrevocably transferred to the trusts by the grantor. Therefore, under the principle in the *Blair* case, the Trusts being the owner of the beneficial interest, the income in the instant case is taxable to the trusts and not to the grantor. Accordingly the decision in the instant case is in conflict with the principle in the *Blair* case.

II. The decision here is in conflict with the decisions of other Courts of Appeals in:

(A) *Commissioner* v. *Bateman*, 127 F. 2d 266, CCA 1.

(B) *Commissioner* v. *Reece*, 233 F. 2d 30, CCA 1.

(A) The *Bateman* case, *supra*, is in conformity with the *Clifford* case *supra*, and the *Blair* case, *supra*, but is contrary to the instant case. In the *Bateman* case the taxpayer created a trust whereby 5% of the annual income was to be retained by the trustee and added to the corpus. The taxpayer retained the power to distribute by Will all of the corpus. The question was whether the taxpayer retained such ownership of the trust so that the 5% accumulated income was taxable to her and not to the trust.

In holding that the taxpayer did not retain such ownership so that the income in issue was taxable to her, the Court stated (Page 253):

"By the trust indenture the taxpayer irrevocably surrendered up control over investment and reinvestment of the corpus, and voting rights to the stock. In no event may she be revested with title to the corpus. She can no longer spend or give away the principal of the income during her lifetime. Assuming she has other property ample for her needs, it still is difficult to deny that as to the property she conveyed to trustees she gave up such substantial rights normally associated with the concept of "full ownership" that she should no longer be deemed in substance the "owner" of the corpus within the rationale of the *Clifford* case."

The facts in the instant case are comparable to those in the *Bateman* case. The taxpayer in the instant case retained no power (except as trustee) to control the corpus of the estate, no part of the corpus was to be revested in the taxpayer, and he had no right to any of the income at any time. In short, here petitioner divested himself of ownership completely and in every respect, so that it can not be said that he was the owner of the trust either in law or in fact.

(B) The case of *Commissioner* v. *Reece, supra*, held that a royalty contract could be assigned and that the future royalties would be taxable to the assignee and not to the assignor, even though the assignment was to the assignor's wife. The Court held that where there was an absolute genuine assignment the income would be taxable to the assignee.

In this case Reece assigned his patent rights to Universal Winding Co. on February 20, 1929. Thereafter a patent was issued to Universal Winding Co. on April 4, 1930. The consideration for the assignment of this patent to Universal Winding Co. was the payment of $2500.00 plus a royalty, and in 1930 he received $7500.00 advance on these royalties. Universal Winding Co. agreed

to and made payments up to December 26, 1935, on which date Reece assigned the entire royalty contract to his wife.

The Court held that since there was an absolute assignment of the contract, even though it was to the wife, and since the assignment was genuine, the income was taxable to the assignee, wife, and not to the assignor, husband.

The Court, in an exhaustive analysis of the subject, stated at page 34:

> "The income in the case at bar is admittedly not income "derived from salaries, wages, or compensation for personal service," for Reece never was in the employ of Universal Winding Co. Therefore, the holding in *Helvering* v. *Eubank* does not apply. In cases of income derived from property, we must accept, in deference to *Harrison* v. *Schaffner*, 1941, 312 U.S. 579, 61 S. Ct. 759, 85 L. Ed. 1055, that where the taxpayer retains the "tree" and purports merely to assign the "fruits" thereof, the fruits remain thereafter, and not only in the year in which the assignment was made, taxable as income of the assignor, on the metaphorical concept that the assignment fails to minimize the assignor's taxable income because it is a futile attempt to attribute the fruits "to a different tree from that on which they grew." (Citing Cases) In cases like *Helvering* v. *Clifford* * * * the question is whether the benefits directly or indirectly retained by the assignor blend imperceptibly "with the normal concepts of full ownership", so that it is reasonable to conclude that the assignor remains "in substance" the owner of the corpus—the "tree"—and therefore that the income therefrom may fairly be attributable to the assignor. * * * "
>
> "Also it is clear that the present case is not ruled by *Helvering* v. *Clifford, supra*, and its progeny, nor by *Harrison* v. *Schaffner, supra*, for as above stated the taxpayer after the assignment of December 26,

1935, retained absolutely nothing relating to the subject matter—not the 'tree,' nor anything which could be said to blend imperceptibly 'with the normal concepts of full ownership.' Since the assignment to Mrs. Reece was not of 'salaries, wages, or compensation for personal service' earned by the taxpayer, the issue is as stated by the Supreme Court in *Commissioner* v. *Sunnen*, 333 U.S. 591, 604 (1948): 'The crucial question remains whether the assignor retains sufficient power and control over the assigned property or over receipt of the income to make it reasonable to treat him as the recipient of the income for tax purposes.' • • • •"

"Our conclusion is that it is impossible to read • • • the code as meaning that Congress intended to tax as 1947 income of this 'individual' taxpayer the payments received during the year by Mrs. Reece from the Universal Winding Co. pursuant to the taxpayer's 'absolute assignment' to her in 1935 of all his rights under the contract of 1929 with the Universal Winding Co. As square authority for this conclusion we may cite *Nelson* v. *Ferguson*, 3 Cir. 1932, 56 F. 2d 121, *certiorari* denied • • •.

In the instant case the taxpayer made an irrevocable transfer to the trust and thereby divested himself of all ownership or control of both the corpus and any resultant income. He effected a transfer of the "tree" in its entirety, including any "fruit."

III. The decision of the Court of Appeals here is in error by reason of the fact that the Court misapplied the controlling applicable rules of evidence.

The Court of Appeals affirmed the Tax Court's decision on the ground that the determination of the Commissioner's deficiency "was presumptively correct and the burden was on the taxpayer to prove otherwise", and that, "the proof was without dispute that the corpus of these alleged trusts belonged to the taxpayer." (Ap. 14a)

In reaching this decision the Court of Appeals failed to apply the rule of evidence that:

> The presumption of correctness of the Commissioner's determination disappears when sufficient evidence to sustain a contrary finding has been introduced.

With respect to the weight to be accorded the doctrine of "presumption of correctness" of the finding of the Commissioner, a leading case is *Crude Oil Corporation of America* v. *Commissioner of Internal Revenue*, 161 F. 2d 809. In that case the Tax Court held that the presumption of delivery of the mail was insufficient to overcome the presumption of correctness of the Commissioner's determination that the tax return was not filed. In passing upon the treatment of evidence by the Tax Court, the Court of Appeals held: (P. 810)

> "We think the Tax Court fell into an error of law. The presumption of the correctness of the Commissioner's finding is one of law. It is not an inference of fact. It disappears when evidence, sufficient to sustain a contrary finding, has been introduced."

A statement of the principle was set forth in *Wiget* v. *Becker*, 84 F. 2d 706, in which case the learned Judge (who wrote the decision here appealed from) had this to say (page 708):

> "The presumption of correctness is in the class of the 'burden of proof presumption.' *Morrison* v. *People of California*, 291 U.S. 82, 54 S. Ct. 281, 78 L. Ed. 664; *Casey* v. *United States*, 276 U.S. 413, 48 S. Ct. 373, 72 L. Ed. 632. The party against whom it is invoked must fail if he does not produce evidence against it. It is often referred to in the books as the true presumption. 'A true presumption is not evidence, though it supplies its place and requires the other party to proceed with the negative. Unless he does he loses;

when he does, the presumption is out of the case, and the issue is open.' *United States ex rel.* v. *Pulver* (C.C.A. 2) 54 F. (2d) 261, 263. See, also, *United States* v. *Le Duc* (C.C.A. 8) 48 F. (2d) 789; *Fidelity & Cas. Co.* v. *Niemann* (C.C.A. 8) 47 F. (2d) 1056; *Del Vecchio* v. *Bowers*, 296 U.S. 280, 56 S. Ct. 190, 193, 80 L. Ed. 229. * * *

The conclusions of law in the instant case show that the lower court gave to the presumption of correctness of the commissioner's finding 'the attribute of evidence in the claimant's favor.' Here, both parties submitted substantial evidence on the issue before the court, and in that state of the record the presumption passed out of the case."

In the case of *Del Vecchio* v. *Bowers*, 296 U.S. 280, the Court, on the question of presumption, stated (Page 285):

"The question is whether, as the court below thought, the presumption has the quality of affirmative evidence. The answer must be that it has not."

In the *Del Vecchio* case the evidentiary question was as to the effect or weight to be given the presumption that death is accidental rather than suicidal. The Court in holding the the doctrine of presumption was not involved, stated (Page 286):

"Once the employer has carried his burden by offering testimony sufficient to justify a finding of suicide, the presumption falls out of the case. It never had and cannot acquire the attribute of evidence in the claimant's favor. Its only office is to control the result where there is an entire lack of competent evidence."

The Court of Appeals apparently regarded the doctrine of presumption of correctness as having the quality of affirmative evidence. This, of course, was erroneous. When the petitioner submitted its evidence—and this was the

only evidence submitted—the presumption "passed out of the case," and the determination could be made only upon the evidence adduced, and without any regard to a presumption.

The petitioner has offered undisputed evidence that neither the trust nor its income belonged to the petitioner (R. 11-12-13) and as a result of such evidence the "presumption" fell out of the case.

The Court of Appeals in sustaining the decision of the Tax Court also failed to follow the rule of evidence that:

> The decision of the Tax Court must be based on substantial evidence.

That substantial evidence is lacking here.

In its decision in the instant case the Court of Appeals quoted *Doll* v. *Commissioner of Internal Revenue*, 149 F. 2d 239. In the *Doll* case the Court of Appeals for the Eighth Circuit quite clearly stated: (page 244)

> "Determination of such fact situation is the exclusive province of the Tax Court and its decision must be upheld if based upon substantial evidence"

In *Commissioner of Internal Revenue* v. *Scottish American Inv. Co.*, 323 U.S. 119, the Court stated: (page 124)

> "And when the Tax Court's factual inferences and conclusions are determinative of compliance with statutory requirements, the appellate courts are limited to a determination of whether they have any substantial basis in the evidence. The judicial eye must not in the first instance rove about searching for evidence to support other conflicting inferences and conclusions which the judges or the litigants may consider more reasonable or desirable. It must be cast directly and primarily upon the evidence in support of those made by the Tax Courts."

See also *Helvering* v. *Kehoe* and cases therein cited—309 U.S. 279.

The Court of Appeals in support of its decision in the instant case states (Ap. A. 14a):

> "Taxpayer asserts that the decision of the Tax Court finds no affirmative evidence in its support. There was, however, the determination of the Commissioner of the deficiencies in taxpayer's income tax returns. This was presumptively correct and the burden was on taxpayer to prove otherwise. The proof was without dispute that the corpus of these alleged trusts belonged to the taxpayer and there were the attending circumstances which, except for certain testimony of the taxpayer and the testimony of the bookkeeper of the concern over which taxpayer had complete control and which the Tax Court was not obliged to credit, conclusively showed that the taxpayer had complete dominion and control, with all the attributes of ownership, over these so-called trust funds. There was, as heretofore been indicated, no evidence that the beneficiaries ever exercised any control over these so-called trust funds."

The evidence introduced here dispels whatever presumption of correctness the determination of the Commissioner had. The Court stated that "the proof was without dispute that the corpus of these alleged trusts belonged to the taxpayer * * *." There is no evidence to support this statement. In fact, all of the evidence and the only evidence offered in this respect is to the contrary.

The undisputed evidence is that the petitioner created the trusts, transferred a fund to the trusts, that the fund was invested and the earnings of the investment were paid to the trusts and that no part of the corpus or earnings were under the control of the petitioner. (R. 10, 12, 13).

There is absolutely no evidence to support the Court's conclusion that the grantor was the owner of the corpus and that he was entitled to receive or control the income of the trusts.

The Court of Appeals further states, ". . . there were the attending circumstances which . . . conclusively showed that the taxpayer had complete dominion and control with all the attributes of ownership over the so-called trust funds." This comment of the Court is simply an assertion and no basis can be found for it in the record, since the only evidence adduced was to the effect that there was no control or dominion by the petitioner over the trust corpus or trust income and that he possessed none of the attributes of ownership.

The Court apparently gave considerable weight to its conclusion that the beneficiaries never exercised any control over the trust funds and considered this to be a material factor in reaching its decision. It is respectfully submitted that the matter of control over the trust funds exercised by the beneficiaries has nothing to do with the issues in the case at bar. Control over the trust funds was delegated to the trustees in their fiduciary capacities as trustees. The question is, did the taxpayer divest himself of dominion and control as an owner of the trust funds, and not whether dominion and control of such funds passed to the beneficiaries, who customarily do not have any control over trust funds—that being the very object of most trusts.

The Court of Appeals erred when it concluded that there was sufficient evidence to support the decision of the Tax Court.

IV. The Court of Appeals erred in concluding that under the decisions in certain cases the taxpayer here must be held to be the owner of the corpus.

The Court of Appeals asserted that (Ap. A. Page 8a) upon the authority of *Commissioner* v. *Sunnen*, 333 U.S. 591; *Helvering* v. *Clifford*, 309 U.S. 331; *Helvering* v. *Horst*, 311 U.S. 112; *Doll* v. *Commissioner of Internal Revenue*, 149 F. 2d 239; and *Yiannias* v. *Commissioner*, 180 F. 2d 115, as a matter of law it is required to hold that the taxpayer should be treated as the owner of the corpus. It is rspectfully submitted that the Court misinterpreted the effect or meaning of these decisions with respect to the case at bar.

These cases do not require or justify such holding, since the facts in these cases are not comparable to the facts at bar.

In *Commissioner* v. *Sunnen*, *supra*, the Court held that notwithstanding the taxpayer's assignment of the rights and contracts to his wife, the taxpayer nevertheless retained substantial interest in the contracts as well as power to control the payment of the royalty to his wife, thereby satisfying the various criteria of taxability as set forth in the *Clifford* and *Horst* group of cases. As reason for this holding the Court there stated as follows: (page 724)

> "As president, director and owner of 89% of the stock of the corporation, the taxpayer remained in a position to exercise extensive control over the license contracts after assigning them to his wife. The contracts all provided that either party might cancel without liability upon giving the required notice. This gave the taxpayer, in his dominant position in the corporation, power to procure the cancellation of the contracts in their entirety. That power was nonetheless substantial because the taxpayer had but one of the three directors' votes necessary to sanction such

action by the corporation. Should a majority of the directors prove unamenable to his desires, the frustration would last no longer than the date of the next annual election of directors by the stockholders, an election which the taxpayer could control by reason of his extensive stock holdings. The wife, as assignee and as a party to contracts expressly terminable by the corporation without liability, could not prevent cancellation provided that the necessary notice was given."

In the instant case, unlike the control which the petitioner had in the *Sunnen* case, the petitioner, Paster, had no control over the trust corpus or over the income earned by the trusts, nor could he deprive the trusts of the income or change or modify the amount under the trust investment contract with the Mayflower Distributing Company. Paster had absolutely no control over whether the trusts would have any income from the investment or its amount.

Neither is the case of *Doll* v. *Commissioner*, 149 F. 2d 239, 33 AFTR 1264, controlling or applicable in the case here. In the *Doll* case the husband and wife claimed they were partners and the Court held that they were not. That was purely a matter of fact and the finding of the Tax Court was there fully supported by the evidence so that the Court of Appeals affirmed the holding of the Tax Court based upon the evidence. This case had nothing to do with trusts or the assignment of income from any trusts or contracts.

Similarly, the case of *Yiannias* v. *Commissioner*, 180 F. 2d 115, does not control the issue here and does not justify the conclusion reached. In the *Yiannias* case the taxpayer transferred his partnership interest to his wife. However, he continued to render the same managerial

services to the partnership as required of him under the terms of the partnership prior to the assignment. In addition, he was not relieved of any of his financial or legal obligations as a partner, which were in existence prior to the assignment. Petitioner's wife rendered no services or furnished no capital to the partnership. Although the petitioner gave notice to the partnership of the assignment to his wife, the record failed to disclose any consent by the partnership to such assignment or that the partnership recognized the wife as a partner. The Court held that the husband did not make a valid and effective assignment of his partnership interest and that he was still a member of the partnership, and, therefore, the income was taxable to him.

In the instant case there is no question of any assignment by Paster of any rights that he had in the Mayflower Distributing Company partnership. His status was merely that of an employee. The income for which he is sought to be taxed was income earned by the trusts by reason of an investment of trust funds in the Mayflower Distributing Company. The investment by the trusts had no effect on Paster's income from the partnership, nor did he by creating the trusts transfer or divert any of his income to the trusts.

Neither does the decision of *Helvering* v. *Clifford*, *supra*, require the holding as a matter of law that under the facts in this case the petitioner must be treated as the owner of the corpus.

The Court of Appeals in its decision on page 13 states: (Ap. A. 13a)

> "The test applied in the *Clifford* case was whether a conveyance by taxpayer in trust for his wife had made 'any substantial change in his economic position,'

309 U.S. at page 336, 60 S. Ct. at page 557, 84 L. Ed. 788. The family relationship does not preclude arrangements between its members which will affect tax liability. * * *"

On the contrary, it is the petitioner's contention that the *Clifford* case requires a holding that the petitioner is not the owner of the corpus, since here the evidence definitely shows that there has been a substantial downward change in the taxpayer's financial economic position.

This Court in considering an issue such as involved here stated in *Commissioner* v. *Sunnen*, 68 S. Ct. 715, at page 722:

> "The crucial question remains whether the assignor retains sufficient power and control over the assigned property or over receipt of the income to make it reasonable to treat him as the recipient of the income for tax purposes."

Since the controlling factor determining ownership of the trust is whether the settlor retains sufficient power and control over the transferred property and income, the Tax Court and the Court of Appeals erred in holding that the trust income here was taxable to the grantor in view of the record disclosing:

1. That the grantor created irrevocable trusts and irrevocably transferred the property to the trusts, and forever divested himself of any dominion or control of the trust corpi or income.
2. That the income of the corpus of the trusts is the sole and irrevocable income of the trusts and cannot be converted or used for the benefit of the grantor.
3. That the Trust Indenture prohibits any of the corpus or income being transferred to or for the benefit of the grantor under any circumstances.

CONCLUSION.

For the foregoing reasons, the petition for writ of certiorari to the United States Court of Appeals for the Eighth Circuit should be granted.

Dated, this 12th day of September, 1957.

Respectfully submitted,

DAVID PREVIANT,
212 W. Wisconsin Ave.
Milwaukee, Wisconsin.

MAURICE WEINSTEIN,
623 N. Second Street
Milwaukee 3, Wisconsin
Attorneys for Petitioner.

APPENDIX A.

OPINION.

UNITED STATES COURT OF APPEALS

For The Eighth Circuit

No. 15,703

Herman Paster, Petitioner,
vs.
Commissioner of Internal Revenue, Respondent.

Petition to Review Decision of the Tax Court of the United States.

[June 21, 1957.]

Maurice Weinstein for Petitioner.

Carolyn R. Just, Attorney, Department of Justice (Charles K. Rice, Assistant Attorney General, and Hilbert P. Zarky, Attorney, Department of Justice, were with her on the brief), for Respondent.

Before Gardner, Chief Judge, and Vogel and Van Oosterhout, Circuit Judges.

Gardner, Chief Judge.

This matter is before us on petition to review a decision of the Tax Court of the United States wherein the Tax Court affirmed the action of the Commissioner of Internal Revenue in determining deficiencies in petitioner's income

tax for the fiscal years ending January 31, 1944, 1945 and 1846 in the respective amounts of $40,768.14, $24,588 and $34,637.69.

In the year 1937 one Samuel Taran took over from taxpayer a business then being operated by him under the name of Mayflower Novelty Company. The business was that of selling and distributing novelty equipment such as juke boxes, pinball machines and bowling alleys. At all times thereafter and until on or about January 31, 1946, the business was operated under the exclusive management and control of taxpayer at which time taxpayer purchased the business and became the sole owner. Income tax returns indicated that the business was that of a partnership composed of Samuel Taran, who was taxpayer's wife's uncle, Taran's nephew, J. H. Nilva, and a trust denominated as "S. H. Taran, J. H. Nilva Trust". Initially taxpayer's compensation was fixed at $35 per week plus 15% of the profits of the business. On some date not definitely shown, possibly late in 1939, taxpayer's compensation for services to Mayflower was increased to $75 per week plus 20% of the net profits and at the close of the fiscal year ended January 31, 1943, Mayflower, according to its books, was indebted to him for services rendered in the amount of $51,511.82.

In the meantime and under date of December 29, 1942, taxpayer executed three instruments entitled respectively "Herman Paster—Trust Agreement for the Benefit of Celia Paster", "Herman Paster—Trust Agreement for the Benefit of Donald Joseph Paster" and "Herman Paster—Trust Agreement for the Benefit of Edward Jacob Paster". In each instrument it was recited that taxpayer had "transferred, assigned, set over and delivered * * * unto himself and Sam Walzer" as trustees "A Ten Thousand ($10,000.00) Dollar interest in the proceeds due Herman

Paster as earnings for services rendered to the Mayflower Novelty Company." Celia Paster is taxpayer's wife and Donald Joseph and Edward Jacob are his sons. Except as to the named beneficiaries and the dates for termination of the trusts the instruments were identical and among other things each instrument recited that the trustees should have full power to sell, buy and manage any property comprising the trust property, "to collect, recover, and receive the income thereof and therefrom", and should not be responsible for any loss or damage which might result from the exercise of judgment or discretion "nor for any moneys or property except such as shall actually and in fact come into their possession" under the instrument; that no part of the income should be used to pay any life insurance premiums on policies on the life of taxpayer; that at least fifteen per cent of the income should be distributed annually to the beneficiary and the remainder distributed or retained as corpus in the discretion of the trustees; that the trusts should terminate on November 18, 1960, in the cases of Celia and Donald Joseph, that date being Donald Joseph's twenty-first birthday, and in the case of Edward Jacob on August 22, 1962, which would be his twenty-first birthday; that in the event of death of the beneficiary distributions were to go to issue, and there being no issue, to heirs at law; that the trustees should "keep and maintain separate books and records covering the trust estate"; that the trust was irrevocable and should not be capable of modification except as in the instrument specifically authorized and directed; that additions to the trust res might be made by taxpayer or others by the execution to that effect by the contributor of an instrument in writing and written acceptance thereof by the trustees, and that each trustee should receive $100 per year as compensation for his services. Each instrument also contained other provisions not here material.

Under date of February 1, 1943, the $51,511.82 credited to taxpayer on Mayflower's books for services rendered was entered in an account entitled "Note Payable—H. Paster". Of the $51,511.82 there was no withdrawal of the $30,000 purportedly assigned by taxpayer to himself and Sam Walzer, his brother-in-law, as trustees under the trust instruments but under date of February 1, 1943 a debit of $30,000 was entered in the "Note Payable—H. Paster" account under the description "trans to Note payable—H. Paster, S. Walzer trust" and under the same date an account entitled "Note Payable—H. Paster, Sam. Walzer Trust" was credited in the amount of $30,000 as "Amt set up as trust investment."

At the close of the fiscal year ended January 31, 1944, and as "Profits accruing to Trusts fiscal year end 1/31/44," 051,519.81 was entered as a credit to the above "Note Payable—H. Paster, Sam Walzer Trust" account. The amount so entered had been taken from a memorandum or tabulation prepared by Walter Johnson, Mayflower's bookkeeper. On this tabulation entitled "Mayflower Distributing Co.—Determination of moneys due others—year 2/1/43-1/31/44," and after Mayflower's "Combined income," together with some limited breakdown thereof, was shown as $245,332.42, the following appeared:

> "In consideration of $10,000.00 invested in business for each of 3 trusts the partnership has agreed to pay 7% of profits to each of trusts in return the original investment to remain in business & not subject to being withdrawn without consent of partnership
>
> 7% due Celia Paster Trust 17,173.27
> 7% due Donald Paster Trust 17,173.27
> 7% due Eddie Paster Trust 17,173.27

21% totals	51,519.81	
14% due H. Paster for services rendered	34,346.54	
Total Amt. due others		85,866.35"

There was testimony that the above tabulation was prepared by Johnson on instructions from Taran and it was shown to Taran before entries were made therefrom in Mayflower's books. Tabulations similar to that indicating "moneys due others" for the fiscal year 1944 were prepared at the close of the fiscal year ended January 31, 1945, and January 31, 1946, form which credit entries to the "Note Payable—H. Paster, Sam Walzer Trust" account were made, the credit under date of January 31, 1945, being shown as "Profits for year end 1/31/45," as $33,879.66 and that under date of January 31, 1946, as "Profits for fiscal yr end 1/31/46," as $31,680.28.

Taxpayer testified that Mayflower and the trustees agreed that in consideration of the trustees permitting the company to retain the corpus of the trusts in the business and agreeing not to withdraw the funds without Mayflower's consent the company would pay to each trust 7% of its annual profit. There was no written contract covering this alleged agreement as to the profit-sharing arrangement either between taxpayer and the trusts, or between Mayflower and the trusts, or between taxpayer and the named beneficiaries. Taxpayer testified in effect that Taran knew of taxpayer's action in creating the trusts and that he consented to the arrangement by which the trusts were to receive in the aggregate 21% of the profits of the business. Taran, however, was not called as a witness, nor was any other member of the partnership called as a witness.

In the regular course of keeping Mayflower's accounts and in the reporting of its income the amounts credited to the "Note Payable—H. Paster, Sam Walzer Trust" account, and as derived from the 21% of the profits due the three trusts and the 14% of the profits due taxpayer were lumped together on Mayflower's books as selling expenses. The income tax returns for all three years in question listed the so-called income to the trusts as "Selling Expenses" along with taxpayer's salary and bonus in contrast to the treatment of interest on loans and finance fees which were deducted as "administrative expenses". The evidence will be further developed in the course of this opinion.

The Tax Court, based on a consideration of all the evidence made the following, among other, findings:

> "We have since examined and re-examined the transcript and the other evidence of record, and taking into account the record as a whole, we are satisfied and have found as a fact that in so far as the side tabulations of moneys or percentages of profits 'due others' for the fiscal years ended January 31, 1944, 1945 and 1946, the entries made on the Mayflower books and the sheets maintained by Johnson or other records relied on herein tend or purport to show that the amounts in question were the income of the trusts and not the income of petitioner, they were shams and did not reflect the truth."

Having found the issues in favor of respondent the court entered its decision determining that there were deficiencies in petitioner's income tax for the taxable years 1944, 1945 and 1946 in the respective amounts of $40,768.14, $24,588 and $34,637.69.

Petitioner in effect urges that the evidence is insufficient to sustain the decision of the Tax Court and that under

the evidence and the applicable law the income held to be taxable to petitioner was in fact income of the trusts which were valid and irrevocable.

In considering the contentions of petitioner we must have in mind the applicable rules relative to the evaluation of the evidence in this class of cases. In the first place, the transactions involved are within a family group and must be subjected to special scrutiny "lest what is in reality but one economic unit to be multiplied into two or more by devices which, though valid under state law, are not conclusive so far as Sec. 22(a) is concerned." *Helvering v. Clifford*, 309 U.S. 331. The Commissioner determined deficiencies in taxpayer's income tax for the years here involved and that determination is presumed to be correct so that before the Tax Court the burden was upon the taxpayer to prove its incorrectness.

There can be no doubt that the funds purportedly transferred to the taxpayer and his brother-in-law, Sam Walzer, as trustees were the funds of taxpayer and at least prior to their purported transfer they constituted income taxable to him. It is axiomatic that income is taxable to the one who is the source of the income and who has control over its disposition and it is of no consequence for taxation purposes that the one who creates or is responsible for the income does not receive it but channels it into the hands of another. Treasury Regulation 111 promulgated under the Internal Revenue Code of 1939, provides in part that:

> "Income of a trust is taxable to the grantor under section 22(a) although not payable to the grantor himself and not to be applied in satisfaction of his legal obligations if he has retained a control of the trust so complete that he is still in practical effect the owner of its income."

In the instant case taxpayer, from a practical standpoint retained complete control of these so-called trusts. The funds were his; he named himself as trustee together with his brother-in-law; the beneficiaries were members of his family, two of them minors; he in effect loaned the funds to a partnership of which he had complete control and in doing so contracted with that partnership as to the terms of the loan. In fact, under the terms of the trust instruments he and his co-trustee were given complete control over the trust funds and while the trust instruments provided for termination of the trusts the alleged agreement with the partnership provided that the funds could not be withdrawn without the consent of the partnership. In making this alleged agreement the taxpayer made it impossible for the trusts to terminate without the consent of the partnership and the book entries warranted the Tax Court in concluding that the corpus of these so-called trusts and the income therefrom were treated by taxpayer as belonging to him.

It is not the function of the Court of Appeals on petition for review of a decision of the Tax Court to try the case de novo. The Tax Court is a fact finding tribunal and in the instant case the determination of whether the alleged transfers of petitioner's funds rendered him immune from income tax liability was one to be made by the Tax Court and that determination should not be set aside by this court unless clearly erroneous. Not only the facts but the inferences that may reasonably be drawn therefrom are in the first instance at least for the Tax Court to determine. *Boehm* v. *Commissioner*, 326 U.S. 287; *Commissioner* v. *Sunnen*, 333 U.S. 591. We think the Tax Court was warrented in holding that the taxpayer should be treated as owner of the corpus of the alleged trusts and the income arising therefrom. *Helvering* v. *Clifford*, supra; *Commissioner* v. *Sunnen*, supra; *Helvering* v. *Horst*, 311

U. S. 112; *Doll* v. *Commissioner of Internal Revenue*, 8 Cir., 149 F.2d 239; *Yiannias* v. *Commissioner of Internal Revenue*, 8 Cir., 180 F.2d 115. In *Helvering* v. *Clifford*, supra, which was appealed from this court, the basic facts were somewhat similar to those in the instant case in that the taxpayer there, as here, attempted to create a trust. In the course of that opinion it is said:

> "Technical considerations, niceties of the law of trusts or conveyances, or the legal paraphernalia which inventive genius may construct as a refuge from surtaxes should not obscure the basic issue. That issue is whether the grantor after the trust has been established may still be treated under this statutory scheme, as the owner of the corpus. See *Blair* v. *Commissioner*, 300 U.S. 5, 12. In absence of more precise standards or guides supplied by statute or appropriate regulations, the answer to that question must depend on an analysis of the terms of the trust and all the circumstances attendant on its creation and operation. And where the grantor is the trustee and the beneficiaries are members of his family group, special scrutiny of the arrangement is necessary lest what is in reality but one economic unit be multiplied into two or more by devices which, though valid under state law, are not conclusive so far as Sec. 22(a) is concerned.
>
> "In this case we cannot conclude as a matter of law that respondent ceased to be the owner of the corpus after the trust was created. Rather, the short duration of the trust, the fact that the wife was the beneficiary, and the retention of control over the corpus by respondent all lead irresistibly to the conclusion that respondent continued to be the owner for purposes of Sec. 22(a).
>
> "So far as his dominion and control were concerned it sems clear that the trust did not effect any substantial change. In substance his control over the corpus was in all essential respects the same after the

trust was created, as before. The wide powers which he retained included for all practical purposes most of the control which he as an individual would have."

In the instant case taxpayer had in effect the same dominion and control over the corpus of these alleged trusts and the income arising therefrom as he had before the trust agreements were executed. There is no evidence that the cestui ques ever exercised any control over the so-called trust funds.

The teaching of the Clifford case was further amplified and emphasized by the Supreme Court in *Commissioner v. Sunnen*, supra. In that case the paramount issue was whether the taxpaper retained sufficient power and control over property allegedly assigned to his wife to make it reasonable to treat him as the recipient of the income for tax purposes. In the course of the opinion it is, among other things, said:

> "It is in the realm of intra-family assignments and transfers that the *Clifford-Horst* line of cases has peculiar applicability. While specifically relating to short-term family trust, the *Clifford* case makes clear that where the parties to a transfer are members of the same family group, special scrutiny is necessary 'lest what is in reality but one economic unit be multiplied into two or more by devices which, though valid under state law, are not conclusive so far as Sec. 22(a) is concerned.'
>
> • • • • • • • •
>
> "The principles which have thus been recognized and developed by the *Clifford* and *Horst* cases, and those following them, are directly applicable to the transfer of patent license contracts between members of the same family. They are guideposts for those who seek to determine in a particular instance whether such an assignor retains sufficient control over the assigned contracts or over the receipt of

income by the assignee to make it fair to impose income tax liability on him.

* * * * * * * * *

"* * * As to the legal foundation of the Tax Court's judgment on the tax consequences of the assignments, we are unable to say that its inferences and conclusions from those facts are unreasonable in the light of the pertinent statutory or administrative provisions or that they are inconsistent with any of the principles enunciated in the *Clifford-Horst* line of cases. Indeed, due regard for those principles leads one inescapably to the Tax Court's result. The taxpayer's purported assignment to his wife of the various license contracts may properly be said to have left him with something more than a memory. He retained very substantial interests in the contracts themselves, as well as power to control the payment of royalties to his wife, thereby satisfying the various criteria of taxability set forth in the *Clifford-Horst* group of cases.

* * * * * * * * *

"* * * Despite the assignments, the license contracts and the royalty payments accruing thereunder remained within the taxpayer's intimate family group. He was able to enjoy, at least indirectly, the benefits received by his wife. And when that fact is added to the legal controls which he retained over the contracts and the royalties, it can fairly be said that the taxpayer retained the substance of all the rights which he had prior to the assignments."

In the instant case not only was the taxpayer in a position to enjoy indirectly the benefits accruing to his wife but also those accruing to his two minor sons.

This court has consistently followed the admonitions of the *Clifford* and *Horst* cases. Thus in *Doll* v. *Commissioner of Internal Revenue*, supra, we said:

"Our immediate concern is (having income taxation in mind) with the third of these rules for construction

of revenue acts—that having to do with the purposes of the taxing act. 'The dominant purpose of the revenue laws (as to incomes) is the taxation of income to those who earn or otherwise create the right to receive it and enjoy the benefit of it when paid' (*Helvering* v. *Horst*, 311 U.S. 112, 119, 61 S.Ct. 144, 85 L.Ed. 75, 131 A.L.R. 655) and this includes 'any economic or financial benefit.' *Commissioner of Internal Revenue* v. *Smith*, 324 U.S. 177, 65 S.Ct. 591. Substance and not form controls in applying income tax statutes and 'the realities of the taxpayer's economic interest, rather than the niceties of the conveyancer's art, should determine the power to tax.' *Helvering* v. *Safe Deposit & Trust Co. of Baltimore*, 316 U.S. 56, 58, 62 S.Ct. 925, 86 L.Ed. 1266, 139 A.L.R. 1513 note 1.

"In view of the rules in the preceding paragraph and of the very broad scope given, in the various revenue acts (here section 22(a) of the 1936 Act, 26 U.S.C.A. Int. Rev. Code Sec. 22(a), to the definition of gross income subject to taxation, the Supreme Court has stated general criteria as aiding in determining tax liability as to income derived from capital, from labor, and from combined capital and labor. Since tax liability on income from capital is based on ownership, the criterion there has to do with possession of attributes of ownership by the taxpayer—such as control by (*Harrison* v. *Schaffner*, 312 U.S. 579, 580, 61 S.Ct. 759, 85 L.Ed. 1055; *Helvering* v. *Horst*, 311 U.S. 112, 119, 61 S.Ct. 144, 85 L.Ed. 75, 131 A.L.R. 655; *Helvering* v. *Clifford*, 309 U.S. 331, 60 S.Ct. 554, 84 L.Ed. 788; *Corliss* v. *Bowers*, 281 U.S. 376, 378, 50 S.Ct. 336, 74 L.Ed. 916) or benefits to him (*Helvering* v. *Horst*, 311 U.S. 112, 119, 61 S.Ct. 144, 85 L.Ed. 75, 131 A.L.R. 655; *Douglas* v. *Willcuts*, 296 U.S. 1, 9, 56 S.Ct. 59, 80 L.Ed. 3, 101 A.L.R. 391).

* * * * * * * *

"A recurring situation is that involving a family group. Usually, a family group is an economic unit. Therefore, as to transactions within such a group

'special scrutiny of the arrangement is necessary lest what is in reality but one economic unit be multiplied into two or more by devices which, though valid under state law, are not conclusive so far as Sec. 22(a) is concerned.' *Helvering* v. *Clifford*, 309 U.S. 331, 335, 60 S.Ct. 554, 84 L.Ed. 788. The test applied in the *Clifford* case was whether a conveyance by taxpayer in trust for his wife had made 'any substantial change in his economic position,' 309 U.S. at page 336, 60 S.Ct. at page 557, 82 L.Ed. 788. The family relationship does not preclude arrangements between its members which will affect tax liability (*Commissioner of Internal Revenue* v. *Branch*, 1 Cir., 114 F.2d 985, 987, 132 A.L.R. 839) but it is 'one of the elements to be considered by the trier of the facts.' *Commissioner of Internal Revenue* v. *Katz*, 7 Cir., 139 F.2d 197, 110.

"We have here a written instrument which is sufficient to create a partnership, both at common law and under Missouri decisions, *Schneider* v. *Schneider*, 347 Mo. 102, 146 S.W.2d 584; *Stone* v. *Guth*, 232 Mo. App. 217, 102 S.W.2d 738. The judgment here is at most an adjudication of what was never in doubt. The existence of such a contract is not determinative of this tax issue. There remains the impact of the test of an analysis of 'all the circumstances attendant on its creation and operation.' *Helvering* v. *Clifford*, 309 U.S. 331, 335, 60 S.Ct. 554, 556, 84 L.Ed. 788. This test must be applied in view of the statutory scheme of taxation prescribed in Sec. 22(a), *Clifford* case, 309 U.S. at page 334, 60 S.Ct. at page 556, 84 L.Ed. 788, and under the special scrutiny arising from the situation that only a husband and wife are parties to the contract. *Clifford* case, 309 U.S. at pages 335-337, 60 S.Ct. at pages 556, 557, 84 L.Ed. 788. The question posed for this analysis is whether this contract caused 'any substantial change in his (petitioner's) economic position.' *Clifford* case, 309 U.S. at page 336, 60 S.Ct. at page 557, 84 L.Ed. 788. The answer is to be found in the pertinent facts. Determination

of such fact situation is the exclusive province of the Tax Court and its decision must be upheld if based upon substantial evidence."

Again in *Yiannias* v. *Commissioner of Internal Revenue*, supra, we said:

"The purpose and intent of the income tax law is taxation to those who earn or otherwise create the right to receive income and a taxpayer may not avoid liability for income tax on his income by assigning the right to receive it."

Taxpayer asserts that the decision of the Tax Court finds no affirmative evidence in its support. There was, however, the determination of the Commissioner of the deficiencies in taxpayer's income tax returns. This was presumptively correct and the burden was on taxpayer to prove otherwise. The proof was without dispute that the corpus of these alleged trusts belonged to the taxpayer and there were the attending circumstances which, except for certain testimony of the taxpayer and the testimony of the bookkeeper of the concern over which taxpayer had complete control and which the Tax Court was not obliged to credit, conclusively showed that the taxpayer had complete dominion and control, with all the attributes of ownership, over these so-called trust funds. There was, as has heretofore been indicated, no evidence that the beneficiaries ever exercised any control over these so-called trust funds. None of them testified; neither did Taran nor Walzer testify. The transactions were given special scrutiny by the Tax Court and the inferences which it drew from all the attending circumstances and its decision that "The profits of Mayflower credited on its books to the 'Note Payable—H. Paster, Sam Walzer Trust' account for each of the fiscal years ended January 31, 1944, 1945 and 1946, were income to petitioner and in so far as the

side tabulations of moneys or percentages of profits 'due others' for each of those years or the entries made on Mayflower's books or the three sheets maintained by Johnson, tend or purport to show otherwise, they are shams and do not reflect the facts" were, we think, fully warranted.

We are of the view that the decision of the Tax Court is abundantly sustained by the evidence and its decision is therefore affirmed.

A true copy.

Attest:

Clerk, U. S. Court of Appeals, Eighth Circuit.

APPENDIX B.

JUDGMENT.

United States Court of Appeals

for the

Eighth Circuit

No. 15703 ..... September Term, 1956.

Friday, June 21 1957.

Herman Paster,

Petitioner,

vs.

Commissioner of Internal Revenue.

On Petition to Review Decision of the Tax Court of the United States.

This cause came on to be heard on the petition to review the decision of The Tax Court of the United States entered August 22, 1956, which affirmed the action of the Commissioner of Internal Revenue in determining deficiencies in petitioner's income tax for the fiscal years ending January 31, 1944, 1945 and 1946 in the respective amounts of $40,768.14, $24,588 and $34,637.69, and was argued by counsel.

On Consideration Whereof, It is now here Ordered and Adjudged by this Court that the decision of the said Tax Court, in this cause, by, and the same is hereby, affirmed.

And it is further Ordered by this Court that the said petition to review, in this cause, be, and the same is hereby dismissed.

June 21, 1957.

APPENDIX C.

OPINION OF TAX COURT.

(Not Printed)

Pursuant to Rule 23(i) we have not printed the Opinion of the Tax Court of the United States since we have submitted nine copies of the Record and the opinion is printed at pages 17 to 41, inclusive, of the Record.

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In the Supreme Court of the United States

OCTOBER TERM, 1957

No. 460

HERMAN PASTER, PETITIONER,

v.

COMMISSIONER OF INTERNAL REVENUE

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Eighth Circuit.

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The findings of fact and memorandum opinion of the Tax Court (R. 17-41) are not officially reported. The opinion of the Court of Appeals (Pet. 1a-15a) is reported at 245 F. 2d 381.

JURISDICTION

The judgment of the Court of Appeals was entered June 21, 1957. (Pet. 16a.) The petition for a writ of certiorari was filed on September 14, 1957. The jurisdiction of this Court is invoked under 28 U.S.C., Section 1254 (1).

QUESTION PRESENTED

Taxpayer purportedly created three trusts for the benefit of his wife and two minor sons, respectively, allegedly assigning $10,000 due him from a partnership to each trust, under an alleged oral agreement with the principal partner that the $30,000 should remain in the business, and that the trusts would receive 21 percent of the partnership profits.

The question presented is whether the record warrants the Tax Court's conclusion, affirmed by the court below, that the arrangement was merely a scheme to split the earnings of the taxpayer for income tax purposes among the members of his family, that taxpayer remained the substantial owner of the trust property, and that the income attributed to the trusts was therefore taxable to the taxpayer.

STATUTE AND REGULATIONS INVOLVED

The relevant portions of Section 22 (a) of the Internal Revenue Code of 1939, and Sections 29.22(a)-21(a), (b), (d), (e), (f), 29.166-1(b), and 29.167-1(b) of Treasury Regulations 111 are set forth in the Appendix *infra*, pp. 12-17.

STATEMENT

Prior to 1937, taxpayer was a salesman of novelty equipment. In the first part of 1937 he borrowed money from Taran, his wife's uncle, and attempted to go into a similar business for himself, but the business was failing within a month, at which time Taran took it over and employed taxpayer to run it

for him at $35 a week and 15 percent of the profits. (R. 17-18.)

The business, first known as Mayflower Novelty Company, and later as Mayflower Distributing Company, bought, sold, distributed, and operated coin-operated machines, apparatus, and devices. It kept its books and filed its returns on the basis of a fiscal year ending January 31st. According to the returns, from the time Taran took over the business until January 31, 1946, when taxpayer purchased the company, it was a partnership with Taran, his nephew Nilva, and a trust referred to as "S. H. Taran, J. H. Nilva Trust" as the partners. During part of 1944 and 1945, Taran was in a federal prison. He was not a citizen of the United States. (R. 18-19.)

On December 29, 1942, taxpayer executed three trust agreements for the benefit of his wife and two minor sons respectively, which instruments, except for the named beneficiaries and dates of termination, were identical. Among other provisions, each recited that taxpayer as "Donor" had "transferred, assigned, set over and delivered * * * unto himself and Sam Walzer" [taxpayer's brother-in-law] as trustees a $10,000 interest "in the proceeds due Herman Paster as earnings for services rendered to the Mayflower Novelty Company." The trusts were to terminate on November 18, 1960, in the case of the wife and eldest son, and on August 22, 1962, in the case of the other son. The instruments provided that the trusts were irrevocable, set forth spend-thrift provisions, gave the trustees broad powers over the trust property, and provided that the trustees should

keep and maintain separate books and records covering the trust estate. (R. 19-20.)

About 1939, taxpayer's compensation had been increased to $75 per week and 20 percent of the net profits. On January 31, 1943, the beginning of the three taxable years in issue, Mayflower's books showed that it owed taxpayer $51,511.82 for services, but taxpayer's drawing account showed a debit balance of $17,443.32. The books showed no withdrawal from the amount owed taxpayer of the $30,000 purportedly transferred to taxpayer and Walzer as trustees of the alleged trusts, but there was a debit entry of $30,000 entered in a "Note Payable—H. Paster" account and a $30,000 credit to an account entitled "Note Payable—H. Paster, Sam Walzer Trust" described as "Amt set up as trust investment." (R. 20-21,)

The amounts here in question involve sums of $51,519.81, $33,879.66, and $31,680.28 credited in the three taxable years ending January 31, 1944, 1945, and 1946 to the trusts, based on memoranda or tabulations prepared by Johnson, Mayflower's bookkeeper, on instructions from Taran. (R. 22.) The tabulation for the first taxable year was entitled "Mayflower Distributing Co.—Determination of moneys due others—year 2/1/43-1/31/44," and after Mayflower's "Combined income," together with some limited breakdown thereof, was shown as $245,332.42, the following appeared (R. 21-22):

> In consideration of $10,000.00 invested in business for each of 3 trusts the partnership has agreed to pay 7% of profits to each of trusts in

return the original investment to remain in business & not subject to being withdrawn without consent of partnership

7% due Celia Paster Trust	17,173.27
7% due Donald " "	17,173.27
7% due Eddie " "	17,173.27
21% totals	51,519.81
14% due H. Paster for services rendered	34,346.54
Total Amount due others	85,866.35

Numerous inconsistent entries relating to the trusts and the amounts shown as "moneys due others" for each of the taxable years were recorded on Mayflower's books, and are detailed in the Tax Court's findings. (R. 23-26.) These entries culminated in a closing debit entry on January 31, 1946, of $110,735.41, under the description "Trans to H. Paster draw in exchange for note". (R. 26.)

In keeping its accounts and in the reporting of its income, Mayflower did not treat the sums in question either as in payment to the trusts for the use of money or as distributions of a percentage of profits based on investment, but as selling expenses. (R. 24-25.)

No books were ever set up or maintained for the three trusts purportedly created by taxpayer under the instruments above. Johnson did maintain in pencil and on ruled yellow worksheet paper what he has denominated as a running account for each purported trust. There was one sheet for each such trust and the sheets were kept by Johnson in his desk. According to these sheets, and aside from original cred-

its of $10,000 each, the aggregate of credits up to and including January 31, 1946, was $124,622.73, or $41,540.91 to each sheet. There were a few entries entitled "deductions" described as for federal and state taxes, insurance premiums, payment on stock pool, or for a railway ticket for the wife; and various other entries under the heading "other trust deductions". (R. 26-28.)

According to explanatory symbols, the items entered in the column headed "other trust deductions" represented amounts paid by Mayflower Distributing Company, Paster Distributing Company, and H. Paster personally. Although they appear as indicated on the so-called trust accounts and were possibly provided by or at the instigation of taxpayer, they were not taken into account in arriving at the $110,735.41, the entry closing out the "Note Payable—H. Paster, Sam Walzer Trust" account on Mayflower's books, as having been transferred to taxpayer "in exchange for note.". (R. 28.)

The entries on the three yellow sheets purport to extend through October 31, 1947. On all three sheets the items entered under dates subsequent to January 31, 1946, in the columns headed "other trust deductions," were by symbols shown as having been paid by Mayflower Distributing Company, Paster Distributing Company, Paster Enterprises, and H. Paster personally. There were no entries on any of the sheets designed to show any payments or additions to the purported trusts after January 31, 1946, of profits payments or distributions by Mayflower, its successor, or successors. (R. 28-29.)

Mayflower's returns indicated a loan of $35,000 in the fiscal year 1944, together with substantial interest expense and finance fees in each of the taxable years. (R. 30.)

The Tax Court held (R. 30-41) that the profits of Mayflower credited on its books to the "Note Payable—H. Paster, Sam Walzer Trust" account for each of the three taxable years were income to the taxpayer, and that insofar as the tabulations of money or percentages of profits "due others" purported to show otherwise, they were shams and did not reflect the facts. The Court of Appeals affirmed. (Pet. 1a-15a.)

ARGUMENT

This case presents a factual question which has been decided adversely to taxpayer by both courts below upon evidence which fully supports their decision. Neither a conflict nor any other basis for further review exists.

1. It is axiomatic that a donor who retains command or other economic benefits of ownership of the donated property remains its real owner for purposes of Section 22(a) of the Internal Revenue Code of 1939, Appendix, *infra*, p. 12. *Commissioner* v. *Sunnen*, 333 U.S. 591; *Helvering* v. *Clifford*, 309 U.S. 331; *Harrison* v. *Schaffner*, 312 U.S. 579; *Helvering* v. *Horst*, 311 U.S. 112. Indeed, where as here we are dealing with an intra-family transfer, "special scrutiny" of the arrangement is necessary lest what is in reality but one economic unit be multiplied into two or more by devices which, though valid under state law, are

not conclusive so far as § 22(a) is concerned". *Helvering* v. *Clifford*, *supra*, p. 335. See also *Commissioner* v. *Tower*, 327 U.S. 280, 287-288.

The record unquestionably warrants the Tax Court's conclusion (R. 31-41), sustaining the Commissioner's determination, that taxpayer remained the substantial owner, during the taxable years, of the business funds which he purported to convey to three trusts created by him for his wife and two minor children. The taxpayer named himself and his brother-in-law as trustees; the trust property consisted of an amount owing to taxpayer by a business partnership which he managed and controlled; the entire amount owing was retained and left in the business, subject to taxpayer's dominion and control; there was no written profit-sharing agreement between the trusts and the partnership; and the portions of the business profits ascribed to the trusts were not distributed to the beneficiary, but like the corpus of the trusts were left in the business subject to taxpayer's control. Moreover, various entries made on the books of the partnership, as well as the tax returns, are inconsistent with taxpayer's contention that he relinquished control of the funds allegedly constituting the trust property. The Tax Court was not of course obliged to attach credence to uncorroborated testimony of taxpayer and his bookkeeper regarding the alleged trusts. *Quock Ting* v. *United States*, 140 U.S. 417. After making a painstaking analysis of all the evidence, it pointed out that "from other records and other portions of the testimony" it was impelled to reject taxpayer's conten-

tions (R. 32), and that "even if we should take petitioner's testimony at its face, it would appear that he or his business was making free use" during the taxable years of the monies allegedly transferred in trust (R. 39). Taxpayer's retention of control over the donated funds, to say nothing of other features relied upon by the courts below, furnishes solid evidentiary support for the Tax Court's conclusion that taxpayer remained the substantial owner of the funds.[1] Under familiar rules governing the scope of judicial review of the Tax Court's findings, af-

---

[1] In the words of the court below (Pet. 8a, 10a):

> In the instant case taxpayer, from a practical standpoint retained complete control of these so-called trusts. The funds were his; he named himself as trustee together with his brother-in-law; the beneficiaries were members of his family, two of them minors; he in effect, loaned the funds to a partnership of which he had complete control and in doing so contracted with that partnership as to the terms of the loan. In fact, under the terms of the trust instruments he and his co-trustee were given complete control over the trust funds and while the trust instruments provided for termination of the trusts the alleged agreement with the partnership provided that the funds could not be withdrawn without the consent of the partnership. In making this alleged agreement the taxpayer made it impossible for the trusts to terminate without the consent of the partnership and the book entries warranted the Tax Court in concluding that the corpus of these so-called trusts and the income therefrom were treated by taxpayer as belonging to him.
>
> * * * *
>
> In the instant case taxpayer had in effect the same dominion and control over the corpus of these alleged trusts and the income arising therefrom as he had before the trust agreements were executed. * * *

firmance of its decision by the court below was clearly justified, and the concurrent finding of both courts below on the factual issue presented is conclusive here. *Comstock* v. *Group of Investors*, 335 U.S. 211, 214; *Corn Products Co.* v. *Commissioner*, 350 U.S. 46, 51.

2. There is no conflict. Whether the creator of a family trust retains control or other attributes of ownership sufficient to stamp him the true owner of the trust property presents a question of fact in each case. Far from being in discord with *Helvering* v. *Clifford*, 309 U.S. 331, as taxpayer asserts (Pet. 4-6), the decision below is in full accord with that decision. The Tax Court there concluded that the taxpayer-husband remained the substantial owner for tax purposes of property transferred in trust for his wife, and this Court held that its conclusion was entitled to affirmance on appeal. The instant case presents an *a fortiori* situation for treating the taxpayer as the substantial owner of the trust property. Nor is there any conflict with *Blair* v. *Commissioner*, 300 U.S. 5, as taxpayer alleges. (Pet. 6-7.) There the taxpayer, the beneficiary of a trust, had parted with substantial as well as titular ownership of his interest; moreover, the case arose under the statutory provisions dealing with the taxability of trust income to the trustees *vis a vis* the beneficiaries (1939 Code Sections 161-162), and it was held that local law was determinative of the beneficiary's power to assign his interest. The case was distinguished in *Harrison* v. *Schaffner*, 312 U.S. 579, involving an issue comparable to that here presented, wherein this Court

reaffirmed the principles enunciated in *Helvering* v. *Clifford*, *supra*. See also *Helvering* v. *Stuart*, 317 U.S. 154, 161-162.

As for the two Court of Appeals cases relied upon by taxpayer for conflict (Pet. 7-10), they are clearly distinguishable on their facts. Suffice it to note that in each the Tax Court had found that the transferor retained no control or other incidents of ownership over the property, and in each case its conclusion was upheld on appeal.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

J. LEE RANKIN,
Solicitor General.

CHARLES K. RICE,
Assistant Attorney General.

HARRY BAUM,
CAROLYN R. JUST,
Attorneys.

OCTOBER 1957.

APPENDIX

Internal Revenue Code of 1939:

SEC. 22. GROSS INCOME.

(a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever.

* * *

* * * * *

(26 U.S.C. 1952 ed., Sec. 22.)

Treasury Regulations 111, promulgated under the Internal Revenue Code of 1939:

Sec. 29.22(a)-21 [As added by T.D. 5488, 1946-1 Cum. Bull. 19, and amended by T.D. 5567, 1947-2 Cum. Bull. 9]. *Trust Income Taxable To The Grantor As Substantial Owner Thereof.*—(*a*) *Introduction.*—Income of a trust is taxable to the grantor under section 22(a) although not payable to the grantor himself and not to be applied in satisfaction of his legal obligations if he has retained a control of the trust so complete that he is still in practical effect the owner of its income. (*Helvering* v. *Clifford*, 309 U.S. 331). In the absence of precise guides supplied by an appropriate regulation, the application of this principle to varying and diversified factual situations has led to considerable uncertainty and confusion. The provisions of this section accordingly resolve the present difficulties of application by defining and specifying those factors which demonstrate the

retention by the grantor of such complete control of the trust that he is taxable on the income therefrom under section 22(a). Such factors are set forth in general in paragraph (b) and in detail in paragraphs (c), (d), and (e), below.

(b) *In general.*—In conformity with the principle stated in paragraph (a) above, the income of a trust is attributable to the grantor (except where such income is taxable to the grantor's spouse or former spouse under section 22(k) or 171) if—

(1) the corpus or the income therefrom will or may return after a relatively short term of years (see paragraph (c)):

(2) the beneficial enjoyment of the corpus or the income therefrom is subject to a power of disposition (other than certain excepted powers), whether by revocation, alteration, or otherwise, exercisable by the grantor, or another person lacking a substantial adverse interest in such disposition, or both (see paragraph (d)); or

(3) the corpus or the income therefrom is subject to administrative control, exercisable primarily for the benefit of the grantor (see paragraph (e)).

* * * *

(d) *Power to determine or control beneficial enjoyment of income or corpus.*—Income of a trust is taxable to the grantor where, whatever the duration of the trust, the beneficial enjoyment of the corpus or the income therefrom is subject to a power of disposition (except as provided in section 167(e) and as hereinafter provided in subparagraphs 1 to 4, inclusive), whether by revocation, alteration, or otherwise, exercisable (in any capacity and regardless of whether such exercise is subject to a precedent giving of notice or is limited to some future date) by the grantor, or any person not having a substantial adverse interest in the beneficial

enjoyment of the corpus or income, whichever is subject to the power, or both. * * *

* * * * *

(e) *Administrative control.*—Income of a trust, whatever its duration, is taxable to the grantor where, under the terms of the trust or the circumstances attendant on its operation, administrative control is exercisable primarily for the benefit of the grantor rather than the beneficiaries of the trust. Administrative control is exercisable primarily for the benefit of the grantor where—

(1) a power exercisable by the grantor, or any person not having a substantial adverse interest in its exercise, or both, whether or not in the capacity of trustee, enables the grantor or any person to purchase, exchange or otherwise deal with or dispose of the corpus or the income therefrom for less than an adequate and full consideration in money or money's worth; or

(2) a power exercisable by the grantor, or any person not having a substantial adverse interest in its exercise, or both, whether or not in the capacity of trustee, enables the grantor to borrow the corpus or income, directly or indirectly, without adequate interest in any case, or without adequate security except where a trustee (other than the grantor or spouse living with the grantor) is authorized under a general lending power to make loans without security to the grantor and other persons and corporations upon the same terms and conditions; or

(3) the grantor has directly or indirectly borrowed the corpus or income and has not completely repaid the loan, including any interest, before the beginning of the taxable year; or

(4) any one of the following powers of

administration over the trust corpus or income is exercisable in a nonfiduciary capacity by the grantor, or any person not having a substantial adverse interest in its exercise, or both: a power to vote or direct the voting of stock or other securities, a power to control the investment of the trust funds either by directing investments or reinvestments or by vetoing proposed investments or reinvestments, and a power to reacquire the trust corpus by substituting other property of an equivalent value.

* * * * *

(f) *Limitations of section.*—Despite the limitations of this section, the grantor of a trust directing the payment or application of the income therefrom in satisfaction of the grantor's legal obligations shall continue to be taxable on the income. The grantor may also be taxable on the income of a trust on the ground that such income is attributable to him in a capacity unrelated to dominion and control over the trust as such as defined in subsections (c), (d), and (e) of this section. Thus, the provisions of this section do not affect the principles governing the taxability of future income to the assignor thereof whether or not the assignment is by means of a trust. Nor, for example, do the provisions of this section affect the applicability of section 22(a) to the creator of a family partnership. See further sections 166 and 167.

* * * * *

Sec. 29.166-1 [As amended by T.D. 5488, *supra*]. *Trusts With Respect to the Corpus of Which the Grantor is Regarded as Remaining in Substance the Owner; Taxable Years Beginning Prior to January 1, 1946.*—* * *

(b) *Test of taxability to grantor.*—Section 166 defines with particularity instances in which the grantor is regarded as in substance the owner of the corpus by reason of the fact that

he has retained power to revest the corpus in himself. * * *

* * * * *

But the provisions of section 166 are not to be regarded as excluding from taxation to the grantor the income of other trusts, not specified therein, in which the grantor is, for the purposes of the Internal Revenue Code, similarly regarded as remaining in substance the owner of the corpus. The grantor is regarded as in substance the owner of the corpus, if, in view of the essential nature and purpose of the trust, it is apparent that the grantor has failed to part permanently and definitively with the substantial incidents of ownership in the corpus.

In determining whether the grantor is in substance the owner of the corpus, the Internal Revenue Code has its own standard, which is a substantial one, dependent neither on the niceties of the particular conveyancing device used nor on the technical description which the law of property gives to the estate or interest transferred to the trustees or beneficiaries of the trust. In that determination, among the material factors are: The fact that the corpus is to be returned to the grantor after a specific term; the fact that the corpus is or may be administered in the interest of the grantor; the fact that the anticipated income is being appropriated in advance for the customary expenditures of the grantor or those which he would ordinarily and naturally make; and any other circumstance bearing on the impermanence and indefiniteness with which the grantor has parted with the substantial incidents of ownership in the corpus.

Thus, the grantor is regarded as being in substance the owner of the corpus if, in any case, the trust amounts to no more than an arrangement whereby the grantor, in the ordering of his affairs, finds it expedient to entrust for a period the title to, and custody or management of, certain of his property to a trustee, the income from

such property to be used by the trustee during such period to make those expenditures which the grantor would customarily or ordinarily or naturally make and to which the grantor chooses to commit himself in advance, while the corpus is to be held intact, for return in due course to the grantor. * * *

* * * * *

Sec. 29.167-1. *Trusts in the Income of Which the Grantor Retains an Interest.*—* * *

(b) *Test of taxability to the grantor.*—The test prescribed by the Internal Revenue Code as to the sufficiency of the grantor's retained interest in the trust income, resulting in the taxation of such income to the grantor, is whether he has failed to divest himself, permanently and definitively, of every right which might, by any possibility, enable him to have such income, at some time, distributed to him, either actually or constructively. * * *

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